



Why Cenovus Energy Inc. May Finally Turn a Profit in 2017

Description

Cenovus Energy Inc. ([TSX:CVE](#))([NYSE:CVE](#)) is a large Canadian oil company that produces oil sands, bitumen, and natural gas; its operations are complemented by the transportation and refining of crude oil into petroleum and chemical products. Cenovus has significant exposure to oil prices and, as such, is a great case study into what may happen in 2017 should oil prices increase according to estimates from the International Energy Agency (IEA) and other economic think tanks.

What oil price increases would mean for Cenovus

Cenovus clearly identifies oil prices as a key profitability driver for the company.

In the 2017 budget overview presentation, Cenovus quantifies the company's exposure to various macroeconomic conditions. For example, if the price of WTI crude were to increase or decrease by a factor of \$10, the company estimates the bottom-line effect to be plus or minus \$650-660 million. For a company that lost approximately \$1 billion in 2016, a \$15-per-barrel oil price increase would be enough to transform the company into a profitable machine given the company's current cost-containment initiatives.

The IEA has identified macroeconomic global factors such as declining crude supplies and robust, growing demand for oil as driving factors supporting a continued oil price rebound in 2017. Investors in Cenovus should watch oil prices closely and think about adding to existing positions or initiating a position should oil prices begin to migrate higher.

Heavy vs. light crude

The light-heavy differential (the price difference between "heavy" oil extracted from the Canadian oil sands and "light" crude extracted from fracking largely in the U.S.) is another key profitability driver for Cenovus. Should the differential decrease by a factor of \$5 (assuming price increases will drive relative price decreases between the two crude varieties), the company's profitability stands to increase by a factor of approximately \$350 million. If the spread widens, the company will lose money.

Foreign exchange considerations

Similarly, the company is exposed to changes in the Canadian/U.S. dollar exchange rate. If the Canadian dollar continues to weaken, the company's profitability will be impacted by a factor of \$190 million for each \$0.05 decrease in the value of the Canadian dollar.

The sensitivity analysis conducted by Cenovus can be very helpful for investors looking at what global macroeconomic conditions mean for companies like Cenovus. In the case of Cenovus, it pays to be aware of what is going on in financial markets and monitor changing conditions accordingly.

The upcoming 2017 fiscal year looks to be shaping up to be a very interesting and potentially profitable year for CVE investors.

Stay Foolish, my friends.

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