Why Cenovus Energy Inc. Was up Over 3% on Tuesday

Description

Cenovus Energy Inc. (TSX:CVE)(NYSE:CVE) announced on Tuesday that it was selling its Pelican Lake project and other assets that produce over 19,000 barrels a day to **Canadian Natural Resources Limited** for $975 million. Multiple analysts have said the sale price was higher than expected and confirm that Cenovus received good value for its assets.

Cenovus, as you may recall, was planning to sell assets to fund its own asset purchase from **ConocoPhillips**, which it announced in March of this year, for $17.7 billion. The money from this sale will allow Cenovus to pay down a portion of the $3.6 billion loan the company needed for the ConocoPhillips purchase.

Cenovus still has more assets it plans to sell as it continues to bring down its debt level. Investors were receptive to the positive news as the stock increased by over 3% in trading on Tuesday to close at $10.28.

How high are the current debt levels for Cenovus?

In the company's most recent earnings, Cenovus had debt of over $13 billion. That's 68% of its equity, which totaled just under $20 billion. In the prior year, Cenovus had debt totaling just $6 billion, and it was only 52% of its equity. As a percentage of equity, Cenovus does not have an incredibly high debt level, although some value-oriented investors might be apprehensive to invest in a company with a debt-to-equity ratio higher than 0.5.

However, when you see a company more than double its debt in a year, that will definitely set off alarms. Especially when investors see it's effectively increasing its exposure to the Canadian oil sands, where many in the industry have struggled or gone bankrupt.

How will the sale impact the company's debt?

If the entire sale of the assets is put towards the company's debt, the debt-to-equity ratio would fall to about 0.63. It is an improvement on the balance sheet, but it is still far from where the company was a year ago. The key will be whether or not the assets that Cenovus purchased from ConocoPhillips prove to be as profitable as originally expected. If the price of oil goes up and Cenovus makes incredible profits, few would even pay attention to the company's moderate debt level.

I believe this is an important sale for two reasons. First, there is more trust from investors that management of the company is following through with what was promised and that it is proceeding with the asset sales reasonably quickly. Second, the asset sales are also believed to be at high prices, perhaps even higher than expected. This will make investors more optimistic that the remaining asset sales might follow a similar trend.

Does this make Cenovus a buy?

Investors have been overly punitive of Cenovus since its ConocoPhillips purchase, and the stock has failed to see any sustained upward momentum in its share price as a result. The sale of these assets could be a turning point and could finally mean the stock price stays out of the $9 range once and for all. For a stock trading at under 70% of its book value, I think Cenovus presents a great buy for investors not afraid to take on some risk.

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