Why Cenovus Energy Inc. Is a "Pound-the-Table" Buy on the Dip

Description

Cenovus Energy Inc. (TSX:CVE)(NYSE:CVE) shares have enjoyed a nice trough-to-peak rally of ~60% since the summer but have since pulled back ~11%.

Although there are many reasons to be afraid of the stock, like its massive debt load, I think deep-value investors with the discipline to think long term could reap major rewards as the business recovers over the next few years.

If you'd missed your chance to buy when the stock was in the single digits this summer, this pullback may be your second chance to back up the truck.

Why is Cenovus worthy of pounding the table?

In many of my previous pieces, I've emphasized how the general public was overly pessimistic of the business, despite offloading a huge amount of non-core assets over a relatively short time span. Following the **ConocoPhillips** asset acquisition (which caused the stock to plunge), management promised to raise cash from the divestiture of non-core assets, and this is indeed what the company has been doing since the deal was announced earlier in the year.

Cenovus has raised ~$3.7 billion from its asset sales thus far, which is slightly less than the $4-5 billion the assets were expected to raise, but I don't think that's worthy of a further sell-off, since shares of Cenovus are already severely undervalued at the $12 level.

The general public is too concerned with the short term

Yes, the ConocoPhillips deal was ridiculously expensive, and it was an extremely aggressive move at the time, but I think the sell-off was way overdone, especially considering the fact that crude has shown signs of stability at US$50 levels, with many pundits forecasting US$60 crude sometime in 2018.

There are many uncertainties that come with investing in Canada's oil patch in general, and I believe Cenovus's history of poorly timed moves may have given investors the idea that the ConocoPhillips deal would be another such move. But I don't think that's the case, especially since the deal happened when foreign investors were repulsed by Canada's oil patch.

There's a lot of debt. The balance sheet isn't in pristine condition, but that's no reason to throw in the towel, especially since management stated it could pay off the debt by offloading other assets. I believe many investors have shunned Cenovus just because of its high debt levels. Combine that with an ugly long-term stock chart, and most investors would take a pass on Cenovus.

Cenovus is trading at a gigantic discount to its intrinsic value

Shares of Cenovus currently trade at a 4.54 price-to-earnings multiple, a 0.8 price-to-book multiple, a 0.8 price-to-sales multiple, and a 5.7 price-to-cash flow multiple, all of which are substantially lower than the company's five-year historical average multiples of 24, two, 1.2, and eight, respectively.

The company is dirt cheap because the general public is overly bearish on the company, and I believe right now is a huge opportunity for you to take a contrarian long-term stance.

Thinking longer term

Cenovus's stake in the FCCL oil sands project (a part of the ConocoPhillips deal) will allow for extremely low-cost bitumen production, which, when combined with an improving oil environment will result in shares of Cenovus rebounding by a great deal over the next five years.

In addition, the solvent aided process (SAP) is a great technology that will allow for even lower costs over the long haul. For those unfamiliar with the SAP, it's a modification of the steam-assisted gravity drainage process, which involves the injection of a natural gas liquid (a solvent) and steam into a reservoir to reduce the steam to oil ratio by as much as ~30%. That's a great deal of money saved and fewer emissions!

Bottom line

It looks like the difficult times at Cenovus are in the rear-view mirror. The company was overleveraged, but that's temporary. The company took a lot of short-term pain with the hopes of achieving a long-term gain. Now that a huge chunk of the foundation is in place, investors should be buying the stock, not selling it, especially since a lot of the short-term pain is already baked in.

Cenovus is a strong buy now and on any further dips.

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Date
2025/07/02
Date Created
2017/11/16
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