This Small Canadian Driller Is the Best Way to Play Higher Oil

Description

The sustained recovery in oil coupled with an increasingly positive outlook for crude has brought the spotlight firmly back on the beaten-down oil patch. While investors flock to load up on names such as **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE), **Crescent Point Energy Corp.** and **Cenovus Energy Inc.**, there is one small Canadian driller that presents a far better opportunity: **Parex Resources Ltd.** (TSX:PXT). It is the only Canadian energy stock that has gained in value since the price of crude collapsed in mid-August 2014, rising by 18% since then.

Parex has a long and enviable history of success, and that can be attributed to its focus on its high-quality assets in Colombia as well as a proactive and expert management team.

Now what?

Parex has enjoyed considerable drilling success since focusing on its Colombian operations in early 2014. So far for 2017, Parex has drilled 14 exploration wells and made 12 oil discoveries. Among the latest is Parex's report that along with partner Colombian government-controlled **Ecopetrol SA**, it has encountered oil at the Coyote-1 well in the Middle Magdalena Valley basin located in the eastern Colombian department of Santander.

Because of the considerable drilling success experienced during 2017 Parex has forecast a 21% year over year increase for its 2018 production with it expecting production of up to 43,000 barrels daily.

Impressively, Parex expects that production to be weighted 99% to crude, meaning that it can take full advantage of higher oil prices, while not being impacted by the ongoing weakness of natural gas.

More importantly, in an operating environment where the outlook for oil remains uncertain because of fears that growing U.S. shale oil production could cause it to fall, Parex's 2018 capital program will be funded by cash flow from operations.

That will leave its pristine balance sheet intact.

You see, Parex, unlike many of its peers such as Baytex, has net debt of $1.7 billion and remains debt free, and it has an undrawn credit facility of $100 million as well as $140 million in working capital. That means it is well positioned to weather any further downturns, while being able to fully benefit from firmer prices should the current rally continue. It also means that the funding is available to rapidly ramp up operations should oil rally further than expected.

The strength of Parex's operations can be seen from its third-quarter 2017 results, where daily production grew by 22% quarter over quarter, and its operating netback — a key measure of operational profitability — shot up by just over US$7 per barrel. That trend should continue, because Parex, unlike Baytex or many other heavily indebted peers, was not forced to sharply pare back investment in its drilling and exploration program because of the prolonged slump in crude.

Parex is also in the position to benefit from higher Brent prices with the international benchmark price trading at an almost US$6 per barrel premium to West Texas Intermediate. That will give Parex's earnings a healthy bump that the majority of its peers are incapable of enjoying.

So what?

While no investment is without risk, Parex's strong operational performance in what can only be described as a difficult operating environment has been impressive. Its ability to grow production and reserves despite sharply weaker oil prices highlights the considerable upside available for investors, making it one of the most attractive plays on higher oil.

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