Cenovus Energy Inc. Is Ready to Unlock Value for Investors

Description

We have entered reporting season again for energy stocks. Tomorrow, much-maligned Canadian oil sands producer **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) will report its first-quarter 2018 results. Let's take a closer look to try and determine what to expect from Cenovus as well as whether it represents an attractive investment in an environment where crude is rising in value.

Now what?

Cenovus has amassed a solid asset base and is focused on its Christina Lake and Foster Creek steam-assisted gravity drainage (SAGD) projects, which have a combined production capacity of almost 400,000 barrels of oil daily. It has also acquired three million acres of land located in Alberta's Deep Basin, which has production capacity of 120,000 barrels of crude daily.

Those assets give Cenovus impressive net oil reserves of 5.4 billion barrels, which have been calculated to have an after-tax net asset value (NAV) of $38 billion. This is equivalent to $31 per share, which is more than double Cenovus's share price, indicating the considerable potential upside available to investors.

Nonetheless, Cenovus, like many oil companies, entered the oil slump that started in late 2014 with a bloated balance sheet. The driller's considerable debt weighed on its performance and share price, as markets feared the worse over the outlook for crude. The company has, however, engaged in asset sales, selling four legacy conventional oil and natural gas assets for $3.7 billion, allowing it to erase a large proportion of that debt.

Cenovus has also been able to significantly reduce expenses, focusing on achieving $1 billion in capital, operating, and general, as well as administrative cost savings over a two-year period. That program was largely completed by the end of February 2018 and should significantly expand Cenovus's margins.

Importantly, the driller's 2018 guidance appears to be on track. First-quarter production is expected to have averaged at least 350,000 barrels daily, which is 49% greater than the equivalent quarter in 2017. That bodes well for a nice bump in Cenovus's bottom line because of significantly higher oil prices.

In fact, Cenovus is on its way to reporting a notable lift in earnings because of oil's sustained rally. West Texas Intermediate (WTI) is trading at US$68 per barrel, which is 31% higher than the US$52 the driller had budgeted for in its 2018 guidance. That means cash flow and its bottom line will grow exponentially over the course of 2018 should higher oil remain in play for a sustained period.

What makes Cenovus a particularly appealing investment is that the driller's breakeven costs have been estimated by analysts to be around US$40 per barrel, emphasizing just how profitable its operations are with WTI at US$68 a barrel.

However, outages at Cenovus's refinery operations during the first quarter 2018 will negatively affect its earnings, although it shouldn't have a significant impact on the company's overall performance.

So what?

After attracting considerable ire from the market for loading up on debt right before oil prices tanked, Cenovus is an increasingly attractive proposition for investors. Its high-quality assets, steadily growing production, and focus on reducing costs coupled with higher oil will give its earnings a healthy lift, and it is not hard to envisage that its first-quarter 2018 results will be strong. That should give its shares a solid boost, making now the time to acquire Cenovus.

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