2 Heavy Oil Producers to Benefit From Higher Oil Prices

Description

The prolonged slump in crude hit Canada's energy patch hard, although the recent rally, which sees the North American benchmark West Texas Intermediate (WTI) trading at over US$67 a barrel, has been a boon for many energy stocks. Two energy stocks that suffered greatly because of the harsh operating environment were **Athabasca Oil Corp.** (TSX:ATH) and **BlackPearl Resources Inc.** (TSX:PXX). This stemmed from them having heavily leveraged balance sheets coupled with unproven operations when the downturn commenced in late 2014. This meant that their cash flow diminished sharply when the oil slump truly set in.

Nevertheless, Athabasca and BlackPearl have performed strongly over the last month to be up by 37% and 32%, respectively, and there are signs that they could very well rally further if higher oil remains in play for a sustained period.

Now what?

Athabasca has oil sands assets located in Alberta as well as light oil operations in the Duvernay and Montney plays, also located in the province. The driller finished 2017 with oil reserves of almost 1.3 billion barrels, which is an impressive five times greater than a year earlier. Those reserves were independently estimated to have an after-tax net asset value (NAV) of $3 billion, which comes to almost $6 per share, or four times greater than its last-traded price.

The marked increase in Athabasca's oil reserves couldn't have come at a better time given the sustained rally in crude since the start of 2018. As WTI rises in value, the NAV of Athabasca's oil reserves will expand, because it was calculated using an average price for WTI of US$58.50 per barrel for 2018 and US$58.70 for 2019, both of which are well below the current market price.

Athabasca has also been able to grow its production, which averaged 35,421 barrels daily for 2017, or almost four times greater than 2016. It was 90% weighted to crude, meaning that the driller is essentially not exposed to the downturn in natural gas. The driller is forecasting that production will grow at a compound annual growth rate (CAGR) of 15% between now and 2020, with 2018 production expected to be at the top estimate 41,000 barrels daily or 16% higher year over year. That will give the company's earnings a solid lift, especially if WTI stays above US$65 per barrel.

BlackPearl owns two conventional heavy oil properties and one steam-assisted gravity drainage (SAGD) project located in Alberta. As at the end of 2017, these properties were estimated to have oil reserves of 162 million barrels, valued, after tax, to be worth $1.7 billion, or $4.67 per share. That is almost three times higher than BlackPearl's share price, which, in conjunction with higher oil prices causing the NAV of its reserves to rise, and the considerable exploration upside of its Blackrod SAGD project, highlights that it is attractively valued.

The Blackrod property is expected to start commercial production somewhere between 2019 and 2021. It is permitted and capable of producing up to 80,000 barrels daily, meaning that when it comes online BlackPearl's earnings will receive a solid bump.

For 2018, BlackPearl has forecast that at its annual production it will average 12,000 barrels, which is 18% greater than 2017. That increase couldn't come at a more opportune time, because when combined with higher oil prices, the company's earnings will receive a solid lift.

So what?

Both companies have been hit hard by oil's prolonged downturn, but their outlooks have brightened considerably now that WTI is trading at over US$65 per barrel. There is every sign that should oil continue to rally, or, at the very least, remain firm for a sustained period, then Athabasca's and BlackPearl's performance will improve significantly, driving their share prices higher.

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