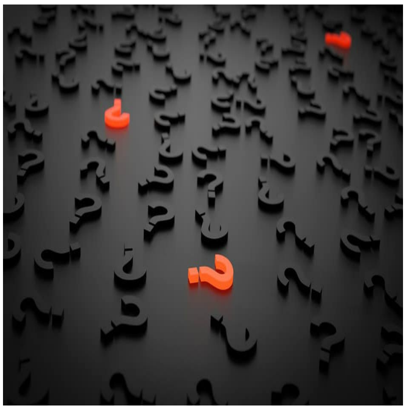

AltaGas Ltd. vs. Cenovus Energy Inc.: Which Energy Stock Is a Better Buy?

Description

AltaGas Ltd. (TSX:ALA) and **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) both reported their 2018 first-quarter results last week. The results of the two energy companies were rather weak overall.

Let’s compare AltaGas to Cenovus Energy to see if either one of these companies deserves a “buy” rating.

AltaGas

After reaching a price over $53 in August 2014, AltaGas is now trading for about half of this value. The stock had a compound annual growth rate of return (CAGR) of -9% over the last three years, and it has dropped 10% since the beginning of the year.

AltaGas reported a first quarter adjusted EBITDA of $223 million, down from $228 million in the same quarter in 2017 and slightly below estimates of $227 million.

The stock has a dividend yield of 8.6%, which is attractive to income investors. AltaGas has increased its dividend every year even when earnings were falling. As a result, the dividend is now about eight times higher than its earnings.

AltaGas relies on its **WGL Holdings, Inc.** acquisition to increase its earnings per share and normalized funds from operations as well as to grow its dividend by 8-10% per year through 2021. EBITDA is expected to rise by 25-30% for 2018 after the closing of the acquisition, which is expected in mid-2018. The natural gas company still needs the approval of the District of Columbia.

The WGL acquisition is expected to drive growth in all three business segments (gas, power, and utilities).

AltaGas’ earnings are expected to grow at an average annual rate of 15.8% for the next five years. This is a big improvement compared to the past five years, during which earnings decreased by 7.7% per year on average.

Cenovus Energy

Cenovus Energy is another energy stock that has been beaten up for quite a long time. After reaching a price near $35 in July 2014, the stock is now trading for about only a third of this value. The stock had a CAGR of about -15% for the last three years, but it has surged 15% since the beginning of the year.

The oil sands producer posted a huge net loss of $914 million in its latest quarter, compared with a profit of $211 million a year earlier. A big part of that loss came from a hedging program on oil prices that caused a $469 million risk management loss. The lack of pipeline capacity has increased the discount buyers take for Canadian oil over West Texas Intermediate (WTI).

Cenovus is considering slowing the development of a 50,000-barrel-per-day oil sands expansion project that it started building early in 2017 if new export pipelines are not built to carry oil out of Alberta.

Due to weak natural gas prices, the company recorded a non-cash asset impairment charge of $100 million for its Clearwater assets.

Revenue was $4.61 billion in the first quarter, which is 30% higher than a year ago and above analyst estimates of $4.2 billion. Oil sands volumes nearly doubled as a result of Cenovus buying assets from **ConocoPhillips** last year for $17.7 billion, which left the energy company with a huge debt. Cenovus is now focused on paying down that debt.

Earnings are expected to decrease at an average annual rate of 5% for the next five years. This means that Cenovus' situation is getting worse, as the company's earnings grew at a rate of 10% per year on average during the past five years.

Bottom line

While AltaGas and Cenovus Energy are both risky investments, I would choose to buy AltaGas over Cenovus for its higher growth perspectives.

While there is some uncertainty surrounding the closing of the WGL acquisition, if things go well, this acquisition is expected to bring significant upside in AltaGas' earnings. So, if you have a high tolerance for risk, it's a good idea to buy some shares to profit from the drop in AltaGas price.

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1. Dividend Stocks
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