



Is Cenovus Energy Inc. (TSX:CVE) a Worthwhile Investment?

Description

Oil's [latest rally](#) as well as the convergence of the price differential between West Texas Intermediate (WTI) and Brent have generated considerable interest in energy stocks.

One that has been garnering considerable attention is beaten-down **Cenovus Energy Inc. (TSX:CVE)** ([NYSE:CVE](#)). The heavy oil producer has seen its market value rise by a mere 5% for the year to date, significantly lagging behind WTI, which has gained almost 20%. Some pundits claim that Cenovus is an attractively valued energy stock that is poised to soar. While there is no doubt that higher crude will act as a tailwind for Cenovus, it appears that there are better investment opportunities in the North American oil patch.

Now what?

For the first quarter 2018, Cenovus reported some disturbing results. While oil and gas production from continuing operations grew almost three-fold compared to a year earlier, driving higher revenue, profitability and net earnings plunged sharply. Cenovus reported a netback of \$5.11 per barrel of oil sold, which was less than a third of the \$16.24 reported for the first quarter in 2017. That indicates there was a significant decline in the company's operational profitability and was among the key reasons for Cenovus reporting a net loss of \$654 million compared to a net profit of \$2.6 billion a year earlier.

The marked deterioration in the profitability of Cenovus's operations can be primarily attributed to the deep discount applied to Canadian heavy oil, Western Canadian Select (WCS), and sharply weaker natural gas prices. While the differential between WCS and WTI [has converged](#) in recent weeks, it remains at just under US\$21 per barrel, which is around US\$3 a barrel lower than it was at the start of the year. That is having a significant impact on Cenovus's profitability, because heavy crude makes up roughly 74% of the company's production.

The other issue is weaker natural gas, which is responsible for the remaining 26% of Cenovus's output. Natural gas, which is trading around US\$3 per million British thermal units (mmBtu), remains caught in a protracted slump, while there are signs that prices could firm further, particularly once winter

commences, a rapid expansion of supply will weigh on prices.

Another factor eating into Cenovus's profitability is that firmer WTI means higher condensate prices, and condensate performs a crucial role for heavy oil producers, because it acts as a diluent, which makes it flow, so it can be transported. This was reflected in a 7.5% year-over-year increase in first-quarter 2018 transport and blending costs. As WTI climbs higher, it will push up the price of condensate, further impacting Cenovus's profitability.

The only bright spot in Cenovus's outlook is that its refining business is returning to full capacity after the completion of turnarounds during the first quarter. That in combination with wider light/heavy crude oil differentials will boost profitability and offset the impact of the deep discount applied to WTI.

So what?

Cenovus certainly isn't my first pick when it comes to playing higher oil. Upstream oil producers such as **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) or **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE), where a considerably portion of their oil output is light and medium crude, are more attractive opportunities. Both possess high-quality light oil acreages, are trading at less than the net asset value of their oil reserves, and are growing production at a steady clip.

CATEGORY

1. Energy Stocks
2. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. NYSE:CVE (Cenovus Energy Inc.)
2. NYSE:VRN (Veren)
3. TSX:BTE (Baytex Energy Corp.)
4. TSX:CVE (Cenovus Energy Inc.)
5. TSX:VRN (Veren Inc.)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Sharewise
4. Yahoo CA

Category

1. Energy Stocks
2. Investing

Tags

1. Editor's Choice

Date

2025/08/28

Date Created

2018/07/06

Author

mattdsmith

default watermark

default watermark