Buy this International Driller to Profit From Higher Oil in 2019

Description

After hitting a multi-year high of over US$86 a barrel back in early October 2018, crude has pulled back sharply to see the international benchmark Brent now trading at just over US$54 per barrel. While this has certainly dampened the outlook for many energy stocks, it doesn't mean that investors should avoid the sector. One relatively low risk high return opportunity is **Gran Tierra Energy Inc.** (TSX:GTE)(NYSEMKT:GTE), which has lost 41% over the last three months, creating an opportunity for contrarian investors.

Oil is expected to rally

It's inevitable that oil will eventually recover for a variety of reasons, but the most important tailwind will be the implementation of OPEC's latest round of production cuts in January 2019. The cartel and its allies have committed to shaving around 1.2 million barrels daily off their oil production; this will likely help drain the global supply glut and balance energy markets. Some analysts are predicting that those cuts could propel Brent to as high as US$70 to US$80 a barrel during 2019. While that does appear somewhat optimistic, it is clear that oil will rebound.

Gran Tierra is attractively valued

Gran Tierra is among the best oil stocks to play higher crude, as it can access international Brent pricing, thereby giving it a financial advantage over its peers operating solely in Canada. Gran Tierra isn't impacted by the discounts applied to Canadian crude benchmarks because of the lack pipeline capacity that's preventing it from reach key refining markets.

There is a wide differential between Brent and the North American benchmark West Texas Intermediate (WTI), which sees the international benchmark trading at a premium of US$8 a barrel at writing. For this reason, Gran Tierra's operations are quite profitable seeing it generate an operating netback of US$37.52 per barrel during the third quarter 2018. That netback, a key measure of operational profitability for an upstream oil producer, was higher than Gran Tierra's peers operating in Canada, indicating the tremendous potential of its existing oil assets.

Considerable oil reserves and growing production

The driller is focused on the Andean nation of Colombia, where it has acreage in the country's three major oil producing basins; Putumayo, Llanos and the Middle Magdalena Valley. That acreage holds reserves of 137 million barrels of oil valued at US$2.5 billion or $8.75 per share, roughly three-times the current market value of Gran Tierra's stock, thereby highlighting the considerable potential upside available.

Notably, particularly in an operating environment where crude is expected to rally, Gran Tierra has consistently demonstrated that it can grow production at a steady clip. For the third quarter, its gross oil output expanded by 11% year over year to an average of 36,170 barrels daily. The driller recently announced that its gross daily production had grown to 40,000 barrels, which is over 10% greater than the average reported for the third quarter. Gran Tierra expects 2019 production to average 40,000 to 42,000 barrels daily, representing 12% to 18% year over year growth and thereby positioning Gran Tierra to fully benefit from oil's anticipated recovery.

Gran Tierra's attractiveness as an investment is enhanced by its solid balance sheet. At the end of the third quarter, it had long-term debt of US$399 million with no debt maturities falling due until 2021. It also has considerable liquidity composed of US$130 million in cash and an undrawn bank credit facility totalling US$300 million.

Why buy Gran Tierra?

The consensus among analysts is that oil will recover once OPEC's latest round of production cuts are implemented. This will act as a powerful tailwind for Gran Tierra's stock, which will be enhanced by growing oil production, the ability to access Brent premium pricing, and a rock-solid balance sheet. For those reasons, Gran Tierra is an attractive contrarian play on oil.

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