This Energy Stock Is Shaping Up as 1 of the Best Plays of 2019

Description

While Colombia is attracting further negative attention because of recent security incidents, President Duque's failed tax reform and a growing fiscal revenue gap upstream intermediate oil producer **Parex Resources** (TSX:PXT) is going from strength to strength. The Colombian-focused oil company, which has 1.6 million acres primarily located in the Andean nation's prolific Llanos Basin, gained 2% over the last year, despite the international benchmark Brent losing 14% over the same period. The increasingly optimistic outlook for crude coupled with the quality of Parex's assets and strength of its operations means that it will soar, despite rising geopolitical risk in Colombia.

Attractively valued

In December 2018, Parex concluded a strategic review, which investigated a range of options for unlocking additional value from investors from the driller's existing operations and assets. As a result of that process, Parex elected to initiate a share buyback with it intending to purchase up to 11.4 million of its outstanding common shares. Management made this decision because they believe that the market is not recognizing the driller's true value.

Typically, a share buyback is an expression of confidence in a company's outlook and helps to bolster the stock price. It is easy to understand management's rationale.

Parex has an impressive history of boosting its oil reserves at a solid clip. Since 2013, the driller's reserves have grown at a compound annual growth rate (CAGR) of 43% to total 162 million barrels at the end of 2017 and are 99% weighted to oil. There are signs that Parex's reserves will expand further because of the Capachos Andina discovery made in September 2018 as well as considerable well development work taken over the course of that year.

Such strong reserve growth has bolstered Parex's ability to expand its production. For the third quarter 2018, the company's oil output reached 45,021 barrels of oil daily, representing a 6% increase over the previous quarter and 24% higher than the same period in 2017.

Parex's ability to access international Brent pricing gives it a financial advantage over those upstream oil producers solely focused on North America. This is because Brent has traded for some time at a higher price than the North American benchmark West Texas Intermediate (WTI). At the time of writing, that premium is a handy US$8 a barrel.

It is this, along with low production as well as transportation expenses, that allows Parex to generate industry-leading netbacks. For the third quarter, it reported a netback of US$44.41 per barrel produced when Brent averaged US$75.84 a barrel for that period. Management anticipates that if Brent averages US$60 per barrel during 2019, then Parex will generate a netback of US$32-34, which bodes well for it to report solid earnings.

For these reasons, Parex has been called a cash flow-generating machine. It has consistently demonstrated that it can generate more than enough cash flow to fund maintenance, development, and growth activities while increasing cash on hand. That means Parex can ramp up exploration and development drilling activity at favourable moments. It also augurs well for higher oil reserves and production while allowing Parex to maintain its pristine balance sheet.

Fortress balance sheet

Parex — unlike many of its peers — has zero long-term debt. This, along with considerable liquidity, including US$361 million in cash at the end of the third quarter and an undrawn US$200 million available from an existing credit facility, leaves it well positioned to weather any sustained downturn in the price of crude.

Why buy Parex?

The increasingly optimistic outlook for crude, supported by **Goldman Sachs's** commodities chief David Currie, who believes that Brent will exceed his 2019 US$67.50 per barrel target, along with strong growth production and a rock-solid balance sheet all point to Parex performing strongly over the course of the year.

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