2 Top Canadian Oil Stocks to Cash In on Higher Crude and 1 to Avoid

Description

Oil's sustained rally since the start of 2019, which saw it gain 47%, has brought investors' attention firmly back on the energy patch and Canadian energy stocks. However, it hasn't triggered a shift of investment capital to Canadian energy stocks because of concerns over the significant headwinds facing oil and that prices could collapse once again.

Nevertheless, with many Canadian energy stocks trailing behind oil, it has created an opportunity for investors to pick up some quality names.

Here are two oil stocks to buy and one to avoid.

Gran Tierra Energy (TSX:GTE)(NYSE:GTE)

Intermediate upstream oil explorer and producer Gran Tierra has severely lagged oil's gains since the start of the year. Whereas the international benchmark Brent has risen by a healthy 47%**,** the driller has only gained 11% since the start of 2019. This has created an opportunity for investors to acquire a quality oil producer well below its net asset value.

Gran Tierra is focused on oil exploration and production in Colombia and Peru. It also recently established in Ecuador, where it secured a 100% working interest in the Chapara, Chanangue, and Iguana Blocks in the Oriente Basin, which is a southern extension of Colombia's Putumayo basin.

That has given Gran Tierra's exploration upside a solid lift. It can leverage off the experience acquired in the Putumayo Basin, where it is a leading acreage holder and oil producer, to maximize its return.

Gran Tierra has forecast that 2019 production will rise by up to 19% to 43,000 barrels daily and that it will generate a notable operating netback of up to US$34.50 if Brent averages US$65 a barrel during the year. What makes Gran Tierra particularly appealing is that the driller's oil reserves have an after-tax value of US$4.77 on a fully diluted basis, which is 76% greater than its current market price, highlighting the considerable upside on offer.

Parex Resources (TSX:PXT)

Parex, which is also focused on Colombia, is one of the very few upstream explorers and producers to survive the oil slump in good shape. It has been able to steadily grow production and, like Gran Tierra, is able to access international Brent pricing, giving it a financial advantage over its North American peers. While its stock has risen by 42% for the year to date, there is still considerable upside ahead.

Parex recently announced that its estimated average first-quarter 2019 oil output was 51,200 barrels daily, which is an impressive 26% higher than for the equivalent period in 2018. That attests to the high quality of its Colombia assets and ability to generate strong cash flows as well as earnings, especially in an operating environment where crude is rising in value.

That will boost earnings in the current favourable operating environment. Parex is also generating an industry leading netback of US$29 per barrel produced at an average Brent price of US$65.

The driller has a spotless debt free balance sheet, which enhances its financial flexibility. Management is focused on delivering solid returns for shareholders and is currently engaged in a share buyback as well as exploring other options to unlock value.

Obsidian Energy (TSX:OBE)(NYSE:OBE)

Intermediate oil producer Obsidian was once known as Penn West Petroleum; after gorging itself on debt to fund a wide range of low-quality acquisitions at the height of the last oil boom, Penn West nearly collapsed when crude bottomed. The driller, after significantly downsizing, divested itself of a considerable amount of assets, thus substantially reducing debt, survived an accounting scandal, and changed its name to Obsidian.

It has attracted considerable interest from investors who believed that it's a deep-value play on higher crude, but every indication is that Obsidian is essentially dead money and will struggle to deliver value. Despite the North American benchmark West Texas Intermediate rallying by 46% since the start of 2019, Obsidian has lost 7%, and there appears to be little upside ahead.

Annual average production for 2019, even at the upper end of its forecast of 27,750 barrels daily, will be 7% lower than the final quarter of 2018. Obsidian's average netback for 2019, which is a key measure of operational profitability, will remain low because of high operating expenses, which are forecast to be $14-14.50 per barrel pumped.

While Obsidian has some quality, high-potential oil acreage, roughly half of its oil reserves are undeveloped. This means the driller will need to invest tremendous amounts of capital to boost production, which is difficult for a company with $497 million in net debt that is a very worrying five times operating cash flow.

Obsidian, despite the claims of some pundits, appears incapable of unlocking value for investors, even if oil rises higher, and the worrying pile of debt will weigh on the company for some time to come, making it a highly unappealing investment.

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1. Energy Stocks
2. Investing

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2. TSX:GTE (Gran Tierra Energy Inc.)
3. TSX:OBE (Obsidian Energy)
4. TSX:PXT (PAREX RESOURCES INC)

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Date
2025/07/21
Date Created
2019/04/26
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