



## Now Is the Time to Buy Vermilion Energy (TSX:VET) and Lock In a 9% Yield

### Description

Oil continues to whipsaw wildly on a mix of good and bad news to see the international benchmark Brent having fallen to under US\$70 a barrel, down by 12% over the last year. This has occurred despite growing supply shortages caused by production outages in Libya and Venezuela, as well as U.S. sanctions against Iran and Venezuela. While the outlook for crude remains mixed, it shouldn't [deter investors](#) from adding upstream oil explorer and producer **Vermilion Energy** ([TSX:VET](#))([NYSE:VET](#)) to their portfolios.

### Robust balance sheet

Vermilion, which owns a globally diversified portfolio of oil and natural gas assets, is one of the few intermediate upstream oil producers to have retained its dividend despite oil's prolonged slump. It hiked its dividend payment in 2018 and is now yielding a very juicy 9.5% after the latest sell-off, which sees Vermilion down by 34% over the last year. That is a testament to the driller's financial strength.

Vermilion, unlike many of its peers, didn't load-up on debt at the height of the last oil boom to fund ambitious drilling programs or the acquisition of questionable assets. Instead, it maintained a solid balance sheet, finishing the first quarter 2019 with \$2 billion of net debt, which is a manageable two times funds from operations (FFO).

### Solid results

Importantly, Vermilion has been able to expand production at a solid clip, growing by an impressive 47% year over year to 103,404 barrels daily for the first quarter.

Vermilion's ability to operate profitably despite the prolonged slump in crude is underscored by its operating netback, growing by almost 1% compared to the equivalent period in 2018 to \$31.50 per barrel. It achieved that despite weaker oil, with Vermilion's average realized price per barrel of \$73.45 being 8% lower than a year earlier.

The geographically diversified nature of Vermilion's operations means that it can offset the impact of the price differential applied between Canadian crude and natural gas prices and the North American West Texas Intermediate (WTI) and Henry Hub benchmarks. That allows the driller to access international Brent pricing for a portion of its production, which, for the first quarter, amounted to 18% of its oil output being referenced to Brent.

This gives Vermilion a handy financial advantage over its peers operating solely in North America, because Brent has been trading at a premium to WTI for some time and is expected to continue doing so for the [foreseeable future](#). Brent is trading at almost US\$9 per barrel higher than WTI.

FFO should continue to grow regardless of weaker oil because of Vermilion's focus on boosting higher value production and controlling costs. Vermilion's self-funding growth and income model means that it can maintain its strong balance sheet. It also has a series of commodity hedges in place, which will protect the driller's earnings should oil remain weak.

## Sustainable dividend

There is considerable concern that Vermilion's dividend and monster 9% yield is unsustainable, particularly in an operating environment where oil remains weak with a mixed outlook. The dividend-payout ratio as a function of the last trailing 12 months of diluted net income is 153%, whereas it is a mere 44% of FFO for the same period. This indicates that the dividend is sustainable, particularly when Vermilion's growing production, earnings, and profitability are considered.

It is, however, vulnerable to a sustained downturn in crude, although the likelihood of that occurring appears minimal after taking growing supply constraints, the risk of production outages, and firmer demand into account.

## Putting it together

Vermilion remains one of the best ways to play higher oil. Its growing production, solid netback, and strong balance sheet highlight its appeal. If investors buy now, they can lock in a very juicy 9% yield.

### CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

### TICKERS GLOBAL

1. NYSE:VET (Vermilion Energy)
2. TSX:VET (Vermilion Energy Inc.)

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