Is Cenovus (TSX:CVE) a Good Buy Ahead of Earnings?

Description

Cenovus Energy Inc (TSX:CVE)(NYSE:CVE) is expected to release its second-quarter earnings later this month. With the stock already up more than 25% since the beginning of the year, the question investors might be asking is whether more of a rally is still to come or if we could see the share price fall again. The company is coming off a strong Q1 that saw the oil and gas company benefit from higher prices of Western Canada Select (WCS).

The good news is that WCS has remained strong, staying above US$40 a barrel for most of the year, which should help contribute to what's likely another improved quarter for the company this month. OPEC announcing it would continue restricting production is also a good sign for the price of West Texas Intermediate (WTI), and although that doesn't necessarily mean a stronger price of WCS, with the discount being lower it could certainly help both commodity prices rise.

Even if it's just an increase in the price of WTI, however, that could have a bullish impact on Cenovus as the stock has seen a strong correlation to it over the past year.

With WTI prices climbing over the past month, so too has Cenovus' share price –a trend that could continue leading up to the company's earnings release. The challenge for the stock will be whether it can reach and stay above the $13 mark.

Over the past year, it has only stayed above that price point for brief periods as Cenovus has seen a fair bit of resistance at those levels. That's where earnings will be a key determinant in whether it will be able to break through that resistance or not.

What should investors expect?

The last time the company released earnings, the stock fell drastically after as a result of missing expectations. In previous earnings' releases, the results have been a bit mixed, but typically there has been a lot of movement on the day of earnings and afterwards.

I'm optimistic that the company can benefit from another quarter of strong oil prices, and if it has found a way to shed some more costs from its financials, that could be enough to help it meet or beat expectations this time around.

Gross margins have increased over the years, and if Cenovus can achieve a similar level to last quarter (37%), then that will help any incremental sales flow through to the bottom line, giving the company a good chance at posting a stronger profit than it did in Q1.

Bottom line: is it a buy?

When considering all the factors, Cenovus certainly looks like a tempting buy today. After all, even if it falls short of expectations this quarter, the stock has generally seen support at around $11 for much of the past year. And so if it does disappoint in Q2, I don't anticipate there being a large sell-off unless something unexpected occurred during the period.

The stock is overdue for a rally, as it's still trading below book value, and a good quarter could be all that it needs to finally gain some much-needed momentum.

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Author
djagielski