This Oil Stock Is on Sale at Less Than Half Price

Description

Crude has firmed once again, as growing demand, geopolitical risks, and emerging supply constraints help to buoy its outlook. The international benchmark Brent has gained 27% since the start of 2019 to trade at over US$66 per barrel, giving energy stocks a boost. One driller that has failed to keep pace with oil is **Gran Tierra** (TSX:GTE)(NYSE:GTE), which has 25% over the same period.

Improving outlook

The company has failed to deliver value for investors for some time because of high geopolitical risk in Colombia, where most of its mineral concessions are located, and operational failures, including production outages. The latest news indicates that Gran Tierra's operations are back on track, and it appears very attractively valued, making now the time to buy.

The company was forced to shutter operations at two of its Putumayo blocks in southern Colombia because of farmer blockades, impacting oil output. It also experienced equipment failures at the Acordionero field in the Middle Magdalena basin, which further negatively affected production. These events saw Gran Tierra estimate that it would lose around 4,500 barrels of oil daily, although it recently announced that the blockades in Putumayo had come to an end and that production had been restored.

Since recommencing operations, Gran Tierra's oil output surged to 34,500 barrels daily, or 5,500 barrels greater than for the previous recorded five-day average, which was 29,000 barrels. It also announced that second-quarter oil production averaged 35,550 barrels daily. The commissioning of Gran Tierra's Acordionero operations is back on track; once complete, it will further bolster oil output.

The driller expects to provide an update on how its 2019 guidance was impacted by the outages in its second-quarter 2019 results, which will be released before August 8, 2019.

Trading at a discount to its oil reserves

While these are positive developments, it is the fact that Gran Tierra is trading at a steep discount to its net asset value (NAV) that makes now the time to buy the driller. Gran Tierra's net oil reserves totalling 115 million barrels have been determined to be worth US$2 billion after tax and the application of a 10% discount rate in accordance with industry methodology. After deducting net debt, that comes to $5.21 per share diluted, which is almost 2.5 times greater than Gran Tierra's current market price, underscoring the considerable upside available.

Operational issues and an overbaked perception of risk, particularly associated with operating in Colombia, are weighing on Gran Tierra's market value. Outages, equipment failures, and other related hazards are par for the course in the oil industry, and Gran Tierra in the past has shown itself adept at managing such risks. The degree of geopolitical and security risk in Colombia is lower than many pundits believe. The largest leftist guerrilla group, the FARC, has demobilized and the current president Ivan Duque is committed to improving the domestic security environment for energy companies.

Oil is an important driver of Colombia's economy. The combination of declining foreign investment, the prolonged price slump, and dwindling reserves have all placed considerable pressure on Bogota and the nation's economic well-being. This underscores just how critical it is for the government to ensure the main oil basins are secure and to protect pipelines, which remain the only economic means of transporting crude in the infrastructure-poor nation.

Foolish takeaway

Gran Tierra has failed to deliver value for investors, despite its impressive portfolio of oil assets, solid balance sheet, and ability to access premium Brent pricing, which gives it a financial advantage over those peers operating solely in North America. The risk/reward equation, however, is shifting in the favour of investors, and the driller is heavily undervalued by the market compared to the NAV of its reserves. Gran Tierra's foray into Ecuador, where it was awarded three blocks in the Oriente Basin, has expanded its exploration prospects and future production potential.

For these reasons, despite the recent operational problems, Gran Tierra is a top play for experienced energy investors seeking to bolster their exposure to crude.

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