2 Dirt-Cheap Oil and Gas Stocks That Could Double in 2020

Description

For long-term value investors, there is no better place to look for bargains than in the energy industry.

Investors have been exiting the sector relentlessly the last few years, leaving many stocks undervalued, especially the ones that have turned themselves around and increased their position and stability.

Decreasing operating costs, increasing liquids productions, and employing better capital management have been among the main themes that energy stocks have been doing in order to position themselves to better attract fresh investment.

There are a number of stocks that have been executing well on their turnarounds, but the top two companies for value investors would be **Advantage Oil & Gas** (TSX:AAV)(NYSE:AAV) and **Birchcliff Energy** (TSX:BIR).

Advantage

Advantage is an exploration and production company that is mainly a natural gas producer. Like many of its Canadian peers, it's been investing a lot of its cash flow to increase its liquids production the last few years to diversify away from solely natural gas production.

In its 2019 guidance, it estimated a 100% increase in liquids production over 2018, and looking at its August production numbers it looks like it will hit those targets.

It estimates liquids will account for 20% of revenue in 2019 and then jump to almost 40% for 2020. At the same time, it wants to decrease its AECO exposure as well.

This plan is ambitious, and if Advantage can succeed, it will have done well to turn itself around and reposition itself in the Canadian market. Its strong hedging strategy also helps it to reduce volatility and give the company more stability.

Currently, Advantage has earnings before interest, taxes, depreciation, and amortization (EBITDA) for the last 12 months of nearly $160 million. Its enterprise value (EV)/EBITDA ratio is just over 4.3 times, making it extremely cheap.

It also has an extremely cheap EV/barrels of oil equivalent per day (BOE/D) at around $14,500, which is on the low end.

If all goes as planned, Advantage could easily get back up to the high end of its 52-week range in the near term and possibly further if oil prices can provide a tail wind.

Birchcliff

Birchcliff is slightly larger than Advantage and is also a primarily natural gas company that will do approximately 22% of its production in 2019 in liquids.

It has been decreasing its operating costs and achieved record low operating costs in the second quarter this year of just $3.17 per barrel of oil equivalent.

Its strong performance so far has allowed it to increase its guidance figures for production this year.

It has an extremely low decline rate of roughly 20% this year; that coupled with its low operating costs allows Birchcliff to increase the cash flow it's generating.

Birchcliff's EV is roughly $1.4 billion, and it will do about 79,000 BOE/D of production in 2019. This gives it an EV/BOE/D of roughly $17,700, slightly more expensive than Advantage. It is, however, cheaper than Advantage on an EV/EBITDA basis though.

At an EV/EBITDA ratio of less than four times, Birchcliff is extremely undervalued. It's also returning some of its capital to shareholders through a dividend that yields nearly 5%.

Bottom line

These two companies are the top opportunities in a sector that is offering a lot of value after being beaten up for so long. Investors would be wise to position themselves now ahead of a full turnaround for these companies, which could be aided by a faster recovery in the sector all together.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. TSX:AAV (Advantage Oil & Gas Ltd.)
2. TSX:BIR (Birchcliff Energy Ltd.)

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