



TFSA Investors: If You Can Stomach This 1 Stock, the Returns Will Be Massive!

Description

At its peak, **MEG** ([TSX:MEG](#)) traded around \$53, which represents a 10 times gain compared to current prices that are slightly above \$5. It has also [attracted the attention](#) of another major oil and gas player.

The company has a 100% interest in over 750 square miles of oil leases in the southern Athabasca region of northern Alberta and is engaged in thermal oil development and production at its 80 section [Christina Lake Project](#).

An interpretation of the numbers

For the nine months ended September 30, 2019, the company reports a mediocre balance sheet with negative retained earnings of \$1.8 billion on \$7.8 billion in assets. Although this is not ideal, I'm not concerned with this as I am with many other oil and gas companies that have absolute retained earnings that are 50% of assets. MEG is at 23%.

Total assets are down \$587 million, driven by decreases in PP&E by \$392 million. Despite this, the company reports cash and cash equivalents of \$154 million, which is a good sign. Many oil and gas companies do not have cash balances and rely on its credit facilities, which can be costly. Total liabilities are down \$530 million, driven by decreases in long-term debt of \$483 million.

Revenues are up significantly from \$2.2 billion in 2018 to \$2.9 billion in 2019. Pre-tax net loss is \$106 million driven by \$615 million in product purchases, which is up from \$200 million the prior year. After-tax loss of \$87 million compared to net profit of \$80 million the prior year.

Cash flows continue to be strong with cash from operations of \$406 million driven by a \$595 million cash adjustment for depletion and depreciation compared to \$341 million the prior year. The company repaid \$393 million in long-term debt, which is good, despite being less than the \$1.3 billion reduction in 2018.

But wait, there's more

Looking at the company's notes to its financials indicate a couple of important items.

Firstly, the company has credit facilities totaling \$1.3 billion, which it voluntarily reduced from \$1.8 billion. The \$1.3 billion facility consists of \$800 million under the revolving credit facility and \$500 million under the Export Development Canada (EDC) facility. The credit facility remains unutilized as of September 30, 2019, and the EDC facility had \$379 million drawn down. The total unutilized amount is \$921 million for an unutilized rate of 71%.

Secondly, the company is essentially a pure-play oil and gas company with 98% of revenues coming from petroleum and 2% coming from power. While this is advantageous during times of high petroleum prices, the lack of diversification will also hurt the company when prices are low.

Thirdly, the company is headquartered in Alberta, which means it will benefit from the reduction in the corporate tax rate from 12% to 8% by January 1, 2022. The company recognized a one-time deferred income tax expense of \$33 million coupled with a deferred tax asset of \$251 million, which it expects to take full advantage of in coming years.

Foolish takeaway

Investors looking to diversify their portfolios and purchase shares of an oil and gas company should consider buying MEG. Despite its negative retained earnings and reliance on petroleum revenues, its revenues continue to grow, it reports significantly underutilized credit facilities, and the company will benefit materially from the reduction in the corporate tax rate.

As energy prices rebound, MEG investors will be rewarded.

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