2 Reasons to Buy Vermilion (TSX:VET) Today and Lock In a 14% Yield for 2020

Description

Oil stocks are back in favour after the recently announced OPEC production deal where the cartel and its partners, notably Russia, agreed to shave a further 500,000 barrels daily off their combined oil output. This has given crude a sold lift with a renewed sense of optimism entering global energy markets, seeing the North American benchmark West Texas Intermediate (WTI) gain a healthy 30% since the start of 2019.

While this has given most energy stocks a solid boost, many Canadian names have failed to make any solid gains. Globally diversified intermediate oil producer **Vermilion** (TSX:VET)(NYSE:VET) has seen its stock plunge by 34% since the start of the year, giving it a monster 14% dividend yield. This has sparked considerable speculation that a dividend cut is on the board, because typically such larger double-digit yields are unsustainable. There are signs, however, that the dividend is sustainable, which, along with Vermilion being very attractively valued after failing to follow crude higher, makes now the time to buy.

On sale

Vermilion's proven and probable oil reserves, after the application of 10% discount in accordance with industry methodology, have been independently assessed to have an after-tax value of just under $7 billion. After deducting long-term debt, leases, and asset retirement obligations, Vermilion's reserves have a net asset value (NAV) of $26.74 per share on a diluted basis.

That represents a juicy 29% premium to Vermilion's current share price, indicating that there is considerable upside ahead, particularly when it is considered that oil continues to rally higher. The value of Vermilion's oil reserves will continue to expand because of higher crude as well as additions from exploration drilling and well development, further emphasizing that now is the time to buy.

Sustainable dividend

After seeing its price collapse by 30% since the start of 2019, Vermilion's dividend is now yielding a very juicy 14%, sparking speculation that such a high yield is unsustainable, and a cut is looming.

Vermilion was one of the very few upstream oil explorers and producers to not only retain its dividend after oil collapsed in late 2014, but it didn't cut the payment, despite crude plunging sharply and entering a prolonged slump. That means Vermilion kept paying its dividend, even when WTI plummeted to below US$30 per barrel in 2016.

Now that WTI is at over US$60 a barrel, there is every likelihood that the payment will be maintained with every indication that the dividend is sustainable. Based on an average 2019 price for WTI of US$56.85 per barrel, Vermilion predicts that it will have a total payout ratio, including capital expenditures and dividends, of just over 100%. The assumed price of WTI is roughly the same as the North American benchmark's average price since the start of 2019 of $56.77. Vermilion expects that ratio to fall to just under 100% for 2020 based on an assumed average WTI price of US$58 per barrel.

On top of that, the driller can dial down capital expenditures if required to preserve its balance sheet and sustain the dividend. The driller has a solid balance sheet finishing the third quarter 2019 with $10 million in cash and long-term debt of just under $2 billion, which is a manageable 1.9 times EBITDA. Furthermore, in early November 2019, Vermilion's CEO confirmed that the dividend was safe, stating that it can be maintained through cost efficiencies.

For these reasons, there is every likelihood that the company will maintain its regular monthly dividend of $0.23 per share, which gives it a monster 14% annual yield.

Foolish takeaway

Vermilion is a very attractively valued play on higher oil, which has a proven history of growing oil reserves and production. When that is considered in conjunction with its sustainable dividend payment yielding a very tasty 14%, now is the time buy.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

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

PARTNER-FEEDS

1. Business Insider
2. Msn
3. Newscred
4. Sharewise
5. Yahoo CA

Category

1. Dividend Stocks
2. Energy Stocks
3. Investing

Date
2025/08/17
Date Created
2019/12/17
Author
mattdsmith