1 Top Contrarian Natural Gas Stock to Buy Today, Despite the Oil Crisis

Description

Oil and natural gas prices have tanked over the last two months, sparking a bloodbath for energy stocks. While the outlook for gas is extremely pessimistic, it shouldn't prevent investors from buying **Canacol Energy** (TSX:CNE). The driller has lost 25% for the year to date, creating an opportunity to acquire a quality energy company, which will benefit from unique market conditions in Colombia, despite the oil crisis.

Quality assets

Canacol has amassed 1.5 million net acres in Colombia in the Lower and Middle Magdalena Basins. That acreage holds proven and probable gas reserves of 624 billion cubic feet. Those reserves have been determined to have an after-tax net present value of US$1.6 billion. After deducting Canacol's long-term liabilities including debt, leases, deferred taxes as well as decommissioning obligations, and adding on cash of US$41 million, it has an after-tax net asset value of $9.45 per share.

This highlights that Canacol is trading at a deep 160% discount to its indicative fair value. This underscores the considerable capital gains ahead for investors once stocks and energy markets rebound.

Favourable market conditions

Importantly, Canacol is in a unique position compared to other natural gas drillers, particularly in North America. There is an emerging energy crisis in Colombia, where gas supplies are incapable of meeting demand. This saw Canacol contractually lock in take-or-pay natural gas prices net of transportation costs of US$4.80 per thousand cubic feet (Mcf) sold. That is two-and-half times greater than the Henry Hub North American benchmark, giving Canacol a handy financial advantage over its peers.

The potential for robust earnings growth enhances Canacol's attractiveness. The driller has forecast sales growth of 110% between the end of 2019 and 2023 to 300 million standard cubic feet daily. This will give earnings a sold boost, particularly when it is considered that Colombia's supply shortage will continue for the foreseeable future, supporting higher-than-spot prices.

Even a sharp economic downturn in the Andean nation will have little impact on those unique market conditions. A dearth of recent major gas discoveries and aging offshore fields with rapidly declining production points to a long-term supply shortfall. That means contracted natural gas prices in Colombia will remain higher than the North American market price for the foreseeable future.

Positive growth outlook

Favourable market dynamics will ensure that Canacol's earnings keep growing. The construction of new pipeline infrastructure giving Canacol greater access to local energy markets will further support that growth. The stability of Canacol's earnings makes it a highly attractive investment in an industry under considerable pressure from weaker prices.

Canacol will generate around US$80 million in free cash flow during 2020, despite the sustained decline in gas prices. It plans to use any excess free cash flow to reduce debt. That further boosts Canacol's appeal by strengthening its balance sheet in an uncertain operating environment.

Foolish takeaway

Natural gas stocks are particularly unappealing investments in the current economic environment. Nonetheless, the unique market conditions that exist in Colombia make Canacol an attractive investment. The driller's growing production and solid fundamentals emphasize its solid fundamentals. Canacol's regular dividend, yielding a juicy 6%, boosts its investment appeal. A conservative 21% payout ratio coupled with Canacol's growing earnings indicates that the payment is sustainable.

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Date
2025/08/23
Date Created
2020/03/31
Author
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