Why Cenovus Energy (TSX:CVE) Stock Is Rallying Almost 10%

Description

Cenovus Energy Inc. (TSX:CVE)(NYSE:CVE) stock is rallying today after releasing first-quarter results were released this morning. While the quarterly report was pretty dismal, the focus today is on the price of oil, which is rallying big-time. Maybe much of the bad news is priced in after the 63% year-to-date drop in Cenovus stock price.

Cenovus Energy stock rallies as oil prices rise

The price of oil is up 32% today, driving energy stocks higher and encouraging investors to see beyond Cenovus Energy's disappointing first-quarter results. And with first quarter cash flow from operations down 71%, there's a lot to see beyond.

The market is therefore putting the results aside today because of the sharp rise in oil prices and also because of the glimmers of hope for the future. This is a company that, before the oil price crash, was in a great position. Free cash flow in 2019 was $1.35 billion and the company was reducing its debt levels dramatically. Today, things are obviously quite different.

Cenovus has cut capital spending and suspended its dividend to preserve liquidity. General and administrative costs have been reduced, the crude by rail program was discontinued, and liquidity has improved. Cenovus now has access to $6.7 billion in credit facilities, which management believes will take it through this "short-term" crisis.

But let's back up and take stock of the bigger picture. Cenovus Energy is still a high-quality business. The company's oil sands operations are still low cost and top quartile. The company still has exposure to its non-operated refining operations in the U.S, which helps mitigate weakness in the upstream business.

Cenovus Energy stock rallies as the company ensures it hasthe liquidity to survive this downturn

Cenovus Energy has taken steps to ensure that the company can survive this downturn. Management has focused on its balance sheet, its credit facilities and on driving down costs for a long time. In the last couple of months, this has been an even greater focus.

Notably, management noted that Canadian banks are being very supportive of the oil and gas industry. Both the federal and provincial governments are saying that liquidity support is coming. For now, Cenovus has $6.7 billion in credit facilities to support it through the crisis.

Cenovus Energy credit ratings are now below investment grade at two of the three credit rating agencies. While this is not a desirable outcome, it can be easily understood considering the macro environment.

Everything that the company has control over is going well. From shoring up its liquidity, to reducing costs, to managing its top quartile operations, Cenovus is doing the right things.

Management estimates that its all-in cash break-even is at $38 WTI oil. On an operating cash flow basis, the break-even is $33 WTI oil. Every $1 below the break-even oil price translates into a $150 million to $180 million hit to operating income.

Foolish bottom line

Cenovus Energy is in the throes of chaos right now, along with the oil and gas industry. Cenovus stock is rallying today as the focus is on soaring oil prices.

But the stock is also rallying as investors are making a decision about whether Cenovus will survive this crisis. I think they are betting on a resounding *yes*.

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