1 Top Canadian Oil Stock to Buy Today and Profit From a 2021 Oil Price Rally

Description

Canadian oil stocks have performed poorly since the start of 2020 because of the latest oil price collapse. In recent days, oil prices have bounced back strongly after the North American West Texas Intermediate (WTI) benchmark price, for the first time ever, plunged into negative territory. The less-than-optimistic outlook for oil, even after the end of the price war between Russia and Saudi Arabia, is weighing heavily on oil stocks.

The extreme weakness of Canadian oil stocks has created a once-in-a-decade opportunity to acquire quality drillers at deep discounts and profit from the coming oil rally. One which stands out for the right reasons is **Frontera Energy** (TSX:FEC). It is extremely attractively valued after losing 58% for the year to date, which is marginally more than Brent's 53%. There is every sign that Frontera will rebound strongly once oil recovers.

Better-than-expected results

Frontera owns a diverse portfolio of oil assets across South America. Its operations are focused on Colombia, but Frontera also has oil acreage in Ecuador, Peru, and Guyana. Despite the impact of the coronavirus pandemic on oil prices Frontera reported some credible results.

The driller's oil production declined by a modest 6.5% year over year to 63,572 barrels daily. This was 97% weighted to oil and other petroleum liquids, allowing Frontera to benefit from the higher international Brent benchmark price.

Despite Frontera's average basket sale price being US$41.65 per barrel, or 28% lower year over year, it still generated a respectable operating netback of US$16.21 per barrel sold. Frontera generated EBITDA of US$44 million, which was around a third of the US$145 million earned a year earlier. Cash flow from operations was almost US$47 million, which was 44% lower year over year.

Frontera reported a net loss of US$386 million for the period. That can be attributed to a large increase in impairment charges of almost US$149 million compared to nil a year earlier. It should be noted that they are non-cash charges and didn't impact Frontera's cash flow.

That is important, because oil production is a capital-intensive industry. You see, numerous non-cash charges being included in net income make cash flow and EBITDA better indicators of a driller's financial health.

Frontera will report weaker second-quarter 2020 earnings, because oil prices did not completely collapse until April.

Solid fundamentals

Frontera is well positioned to endure the current harsh operating environment. It is one of the few Canadian oil stocks to finish the first quarter 2020 with a solid balance sheet. That includes a massive pile of cash totalling US$265 million and a working capital surplus of US$68 million.

Frontera's debt of US$364 million is a very manageable 0.6 times EBITDA. This indicates it would take a considerable decline in earnings to place Frontera in the position where it couldn't service its exiting debt and related financial obligations.

In response to the difficult operating environment, Frontera slashed capital spending, is implementing cost reductions, and shuttering uneconomic wells. That will allow the company to preserve its solid balance sheet and emerge from the crisis in solid shape.

Frontera will not pay a dividend, because Brent won't average more than US$60 per barrel for some time, further protecting its balance sheet.

Foolish takeaway

Canadian oil stocks are extremely attractively valued. For the reasons discussed, Frontera is one of the best plays on firmer oil prices. Frontera's appeal is significantly enhanced by it trading at a deep 182% discount to the net asset value of proven and probable oil reserves of around $11.50 per share. That underscores why now is the time buy and the considerable capital gains ahead once oil rallies.

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1. Energy Stocks
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Author
mattdsmith