Why Cenovus Energy (TSX:CVE) Rose 8% Last Week

Description

Cenovus Energy (TSX:CVE)(NYSE:CVE) stock rose approximately 8% last week, going from $23.3 at the start of the week to $25.15 at the end. It was a big rally for a stock that hadn't moved much since June. In the first half of this year, oil stocks rallied to incredible highs, as oil prices gained. In June, the gains started to fade as oil prices came down.

Last week was Cenovus's biggest rally since June. The stock is still down from its all-time highs, but it's climbing rapidly. It remains to be seen whether oil prices will re-take their 52-week highs, but CVE stock has significant potential, even if that doesn't happen. In this article, I will explore the factors that took Cenovus stock higher last week, beginning with the most obvious: oil prices.

Oil prices gain

The price of West Texas Intermediate (WTI) crude oil (North America's most watched oil benchmark) rose last week, going from US$89.57 to US$93.06, a 4% gain. This price gain has implications for oil companies like Cenovus. CVE is a fully integrated energy company, meaning that it extracts, refines, transports and sells oil. It also sells gasoline directly to customers at Husky Energy gas stations.

Oil-related business activities become more profitable the higher the price of oil goes. Particularly if the company doing them keeps costs under control, which Cenovus is doing. In the first and second quarters, Cenovus retired billions of dollars' worth of debt, which reduced its interest costs. As a result, it will be able to deliver higher profits in the future. The debt reduction provides the potential for profits to rise even if oil just stays flat and amplifies the effect of profit gains from rising oil prices.

Solid earnings

The fact that higher oil prices are benefitting Cenovus Energy can be seen in its most recent quarterly earnings release. In the second quarter, CVE earned

- $19 billion in revenue, up 80%;

- $2.4 billion in net income, up 981%; and
- $2.9 billion in cash from operations (a cash-only profit measure), up 118%.

It was a solid quarter. And Cenovus will keep putting out more quarters like it if the price of oil continues to rise. This year, the world is going through an energy crisis, with Germany in particular facing a massive increase in home heating costs. If this situation persists through the winter, then there's going to be a scramble for petroleum products, including natural gas, which is one of the commodities CVE produces. That could lead to even higher earnings in the fourth quarter.

Foolish takeaway

As I've shown, Cenovus Energy rallied last week mainly, because the price of oil went up. CVE's 8% gain was ahead of the 4% gain in oil prices, but remember that oil companies' earnings don't respond linearly to oil price gains. Energy companies have costs. The rise in profit as sales move ever further above costs is faster than the rise in sales itself. So, it's only natural that CVE gained 8% last week. Expect more of it if the world's energy crisis persists.

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