



# Vermilion Energy Inc. (VET)

Updated December 24<sup>th</sup>, 2019 by Samuel Smith

## Key Metrics

<b>Current Price:</b>	\$16.26	<b>5 Year CAGR Estimate:</b>	16.9%	<b>Market Cap:</b>	\$2.5B
<b>Fair Value Price:</b>	\$21.40	<b>5 Year Growth Estimate:</b>	3.0%	<b>Ex-Dividend Date:</b>	12/30/19
<b>% Fair Value:</b>	76%	<b>5 Year Valuation Multiple Estimate:</b>	5.6%	<b>Dividend Payment Date:</b>	1/15/20
<b>Dividend Yield:</b>	13.1%	<b>5 Year Price Target</b>	\$25	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	C	<b>Last Dividend Increase:</b>	N/A

## Overview & Current Events

Vermilion Energy was founded in 1994. Today, the \$2.5 billion market capitalization company is based in Canada and is engaged in the exploration and production of oil and natural gas. The company has operations in Canada, the U.S., Australia, France, Ireland, Germany, and the Netherlands. Vermilion primarily focuses on light oil and liquids-rich natural gas resource plays in Canada and the U.S., natural gas opportunities in the Netherlands and Germany, and oil drilling in France and Australia. In the most recent quarter, Vermilion generated 59% of its output from Canada.

In late October, Vermilion reported (10/31/19) financial results for the third quarter of fiscal 2019. Revenue tumbled on weaker than-expected production levels and disappointing commodity pricing. Petroleum and natural gas sales fell by 23% year-over-year, and fund flows from operations per share fell by 18.7% year-over-year as average production declined to 97.2K boe/day as a result of plant turnarounds, unplanned downtime, and poor weather.

Management reiterated its commitment to sustaining its balance sheet and dividend over pursuing aggressive growth capital expenditures. Due to declining results, the company announced that it would be tightening its belt on its capital expenditure budget, trimming \$10 million from its 2019 capital spending plan, while also gutting nearly all of its growth capital expenditures for 2020.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>FCF/S</b>	---	---	-\$1.09	\$0.61	\$1.09	\$1.09	-\$0.62	\$2.20	\$2.23	\$2.48	<b>\$2.14</b>	<b>\$2.48</b>
<b>DPS</b>	\$1.73	\$1.73	\$1.73	\$1.73	\$1.82	\$1.96	\$1.96	\$1.96	\$1.96	\$2.09	<b>\$2.12</b>	<b>\$2.12</b>
<b>Shares<sup>1</sup></b>	80.6	83.2	92.3	99.3	102.5	107.2	109.6	115.7	123.5	153.9	<b>158.0</b>	<b>170.0</b>

Vermilion's free cash flow-per-share has fluctuated wildly over the past decade. This should not come as a surprise, as oil and gas producers are highly exposed to the price of oil and natural gas. Future growth will be fueled by production growth and higher commodity prices, which are very difficult to predict. In addition to higher expected future commodity prices, Vermilion's acquisition of Spartan is a major growth catalyst. This was the largest acquisition in the history of the company and gives Vermilion greater exposure to the high-quality properties of southeast Saskatchewan. Given the strong production growth and higher expected commodity prices, but also the wild fluctuation of free cash flow-per-share, we find it prudent to expect Vermilion to post free cash flow-per-share around \$2.48 in 2024. One important item to note is that the company has hedged a considerable portion of its commodity exposure over the next several years. This should improve free cash flow stability considerably relative to its past.

## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
<b>Avg. P/FCF</b>	---	---	---	76.6	48.4	55.0	---	15.3	15.9	13.0	<b>7.6</b>	<b>10.0</b>
<b>Avg. Yld.</b>	7.0%	4.9%	5.0%	4.4%	3.8%	4.5%	6.9%	4.6%	5.6%	6.5%	<b>13.1%</b>	<b>8.5%</b>

Vermilion's valuation multiple has fluctuated over the past 10 years, which is not surprising for a cyclical oil and gas production company. Given the current pricing challenges in the oil and natural gas segments, we see fair value at 10

1. In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



# Vermilion Energy Inc. (VET)

Updated December 24<sup>th</sup>, 2019 by Samuel Smith

times free cash flow, which compares favorably to the current valuation of 7.6 times free cash flow. As a result of the volatility of Vermilion’s earnings and cash flow, we believe it is best to conservatively estimate fair value. If the stock returned to 10 times free cash flow, the corresponding move would produce a 5.6% tailwind to Vermilion’s annual returns.

While the price-to-FCF ratio of the stock may seem low to most investors, they should note that this is a small-scale oil and gas company (its output is less than 3% of the output of Exxon Mobil). As such it has a much higher inherent risk than the well-known oil majors, which are much more diversified and integrated. The company also has a weaker balance sheet, bringing with it greater risk.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	---	---	---	284%	167%	180%	---	89%	88%	84%	99%	85%

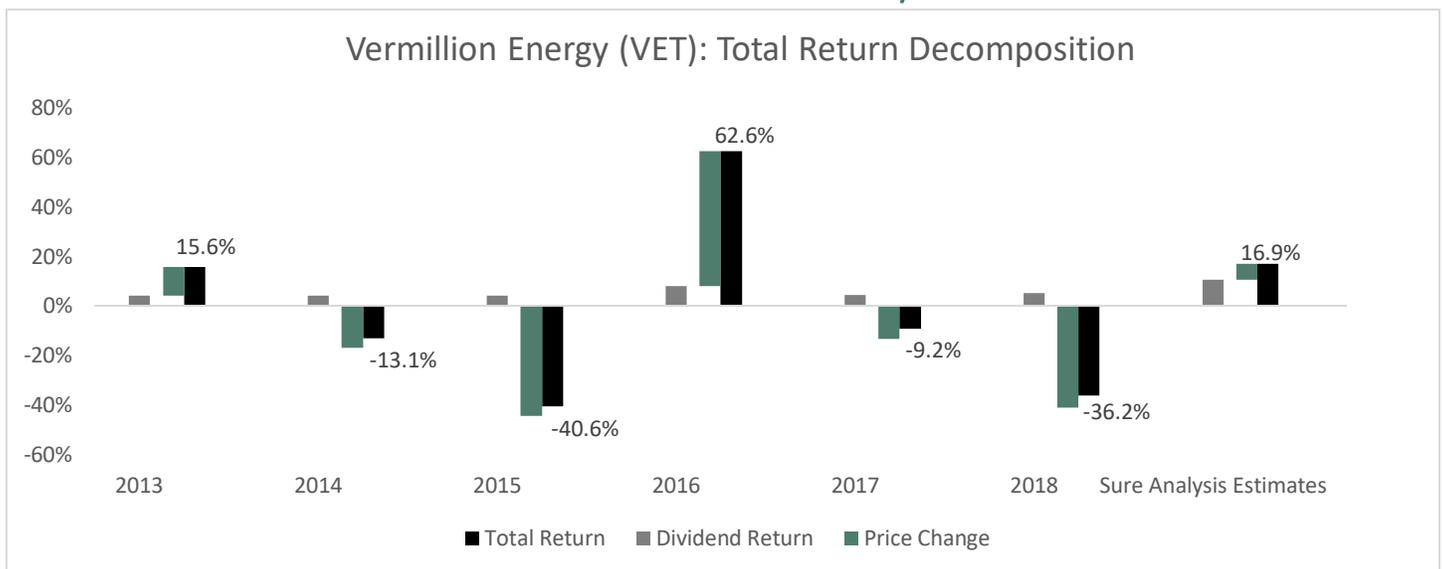
Vermilion may not be the best stock selection for investors primarily concerned with safety and quality, due to the company’s highly volatile fundamentals. The company’s interest coverage and payout ratio will fluctuate a great deal, depending on whether commodity prices are high or low. No oil and gas company can control the direction of commodity prices, which means investors cannot rely on Vermilion as a safe investment.

With that said, the company does have competitive advantages, mainly its oil and gas properties, which have low rates of decline and significant amounts of reserves. This allowed the company to grow production by 15% per year from 2013 to 2019. The company performed surprisingly well during the Great Recession, remaining profitable in 2008 and 2009. If oil and gas prices remain at a decent level, the company could perform well during the next recession.

## Final Thoughts & Recommendation

Vermilion is not a suitable choice for risk-averse investors looking for stability and consistency, as the company’s fortunes will rise and fall based largely on the price of oil and gas. With that said, investors interested in a high dividend yield and growth potential could be interested in Vermilion, particularly if oil and gas prices rise in the coming years. In the absence of a downturn, Vermillion could offer a 16.9% average annual return over the next five years. In a stable operating climate, we view the stock as undervalued, with a high yield and FCF growth. We therefore rate it as a buy.

## Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

1. In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



# Vermilion Energy Inc. (VET)

Updated December 24<sup>th</sup>, 2019 by Samuel Smith

## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	563	706	988	1031	1171	1188	685	626	790	1178
SG&A Exp.	43	75	110	115	136	156	134	122	123	127
Operating Profit	75	226	451	410	509	414	21	-79	80	281
Operating Margin	13.4%	32.1%	45.7%	39.8%	43.4%	34.8%	3.0%	-12.6%	10.2%	23.9%
Net Profit	163	43	144	191	318	244	-170	-121	48	210
Net Margin	29.0%	6.1%	14.6%	18.5%	27.2%	20.5%	-24.9%	-19.3%	6.1%	17.8%
Free Cash Flow	-109	391	-96	-62	140	-105	-56	127	190	17
Income Tax	-1	78	175	163	246	166	3	-48	48	64

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	1978	2325	2679	3092	3483	3778	3033	3031	3161	4604
Cash & Equivalents	94	146	230	103	366	104	30	47	37	20
Accounts Receivable	111	147	173	181	157	148	116	98	132	191
Inventories	5	11	14	26	16	8	9	11	14	20
Total Liabilities	992	1280	1375	1666	1871	2037	1694	1861	1934	2536
Accounts Payable	188	252	292	302	252	257	179	135	174	330
Long-Term Debt	152	303	366	645	930	1067	1000	1010	1010	1319
Shareholder's Equity	986	1046	1304	1426	1612	1741	1339	1171	1227	2068
D/E Ratio	0.15	0.29	0.28	0.45	0.58	0.61	0.75	0.86	0.82	0.64

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	9.5%	2.0%	5.8%	6.6%	9.7%	6.7%	-5.0%	-4.0%	1.6%	5.4%
Return on Equity	20.4%	4.2%	12.3%	14.0%	20.9%	14.6%	-11.1%	-9.6%	4.0%	12.7%
ROIC	16.5%	3.5%	9.6%	10.2%	13.8%	9.1%	-6.6%	-5.3%	2.2%	7.5%
Shares Out.	80.6	83.2	92.3	99.3	102.5	107.2	109.6	115.7	123.5	153.9
Revenue/Share	6.99	8.49	10.71	10.39	11.43	11.08	6.24	5.41	6.46	8.27
FCF/Share	-1.35	4.70	-1.04	-0.63	1.37	-0.98	-0.51	1.10	1.55	0.12

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

### Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.