



Vermilion Energy Inc. (VET)

Updated March 23rd, 2021 by Samuel Smith

Key Metrics

Current Price:	\$8.7	5 Year CAGR Estimate:	12.9%	Market Cap:	\$1.5B
Fair Value Price:	\$10.0	5 Year Growth Estimate:	5.5%	Ex-Dividend Date:	N/A
% Fair Value:	87%	5 Year Valuation Multiple Estimate:	2.9%	Dividend Payment Date:	N/A
Dividend Yield:	0%	5 Year Price Target	\$13	Years Of Dividend Growth:	0
Dividend Risk Score:	D	Retirement Suitability Score:	B	Last Dividend Increase:	N/A

Overview & Current Events

Vermilion Energy was founded in 1994. Today, the \$1.5 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 March, Vermilion reported (03/08/21) financial results for the fourth quarter of fiscal 2020. The company's FFO came in at \$135 million. FCF in Q4 came in at \$75M, which went toward debt reduction. Revenue came in at \$316.2 million. Meanwhile, indicating the impact from a capital program executed predominately during the first part of 2020 with drilling activity over the second half of the year, the average production in Q4 stood at 87,848 boe/d.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
FCF/S	-\$0.46	-\$0.14	\$1.43	\$0.78	-\$0.28	\$1.14	\$1.94	\$1.48	\$1.83	\$0.80	\$1.34	\$1.75
DPS	\$1.73	\$1.73	\$1.82	\$1.96	\$1.96	\$1.96	\$1.96	\$2.09	\$2.12	\$0.43	\$0.00	\$0.90
Shares¹	96.4	99.1	102.1	107.3	112.0	118.3	122.1	152.8	156.6	158.9	158.9	165.0

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 massive headwinds which faced the company last year stemming from the oil price war and the economic disruption from the coronavirus outbreak, we expect the company's free cash flow to recover sharply this year. We also think that the dividend will recover in the years to come, though it will take a long time to recover to its pre-pandemic levels as management will need to retain a lot of cash to shore up the balance sheet and catch up on capex programs.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/FCF	---	76.6	48.4	55.0	---	15.3	15.9	13.0	7.6	2.9	6.5	7.5
Avg. Yld.	5.0%	4.4%	3.8%	4.5%	6.9%	4.6%	5.6%	6.5%	13.1%	13.9%	---	6.9%

Vermilion's valuation multiple has fluctuated significantly over the past 10 years, which is not surprising for a cyclical oil and gas production company. Given the recent challenges, the weakened long-term outlook for the oil and natural gas segments, and Vermilion's considerable leverage, we see fair value at 7.5 times free cash flow (down from 10 times free cash flow prior to the pandemic), which makes shares undervalued at present.

While the fair value estimated 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

1. In millions.

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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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Payout	---	284%	167%	180%	---	172%	101%	141%	116%	54%	---	51%

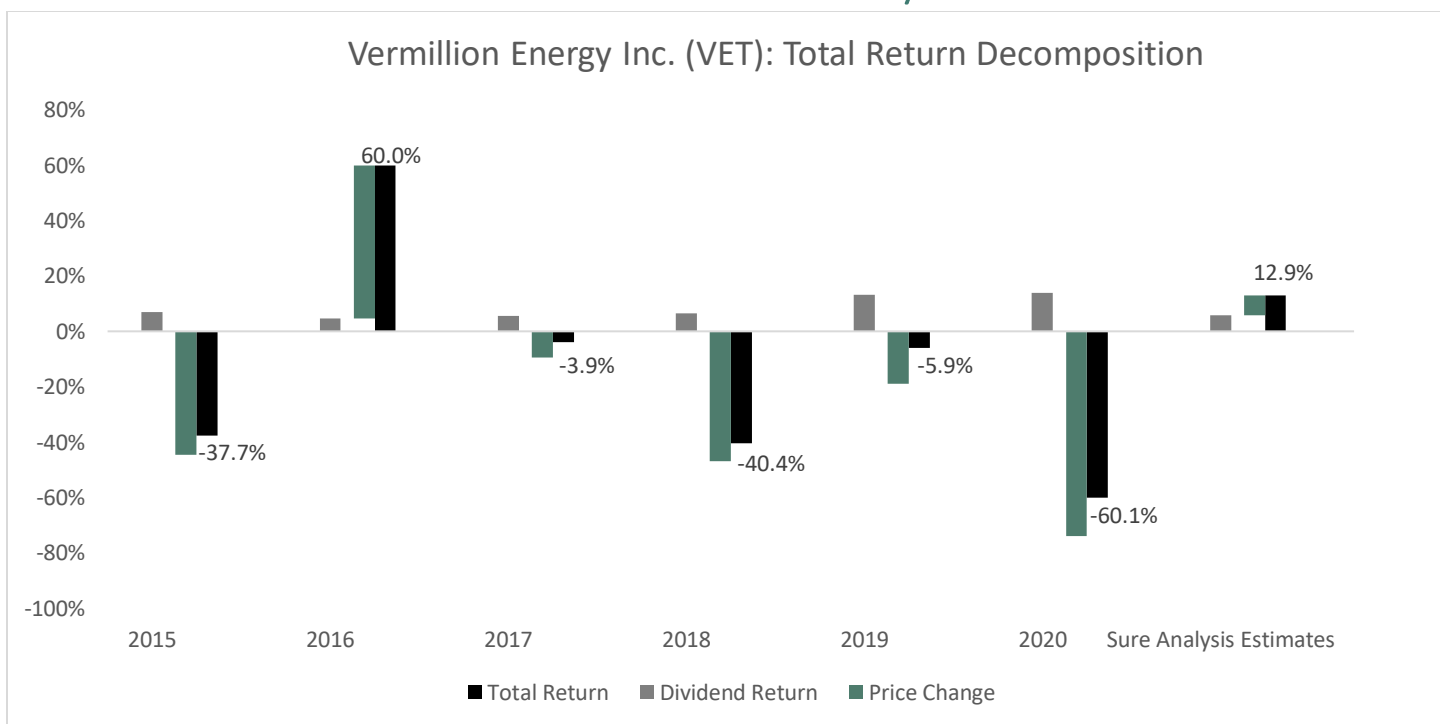
Vermilion may not be the best stock selection for investors primarily concerned with safety and quality, due to the company's highly volatile fundamentals. The company's interest coverage and payout ratio will fluctuate a great deal, depending on whether commodity prices are high or low. No oil and gas 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 can stay at a decent level, the company should be able to weather a recession well. However, last year punished the company's balance sheet due to the collapse in energy prices. As a result, we think that the company will be hesitant to raise its dividend moving forward until they have plenty of coverage with free cash flows and their balance sheet leverage is reduced considerably.

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, and the balance sheet has a lot of leverage at present. Given the lingering challenges and uncertainty facing the company, the annualized total return potential of 12.9% over the next five years should still be viewed with caution by conservative income investors, though we rate the stock a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	1,043	1,083	1,237	1,286	736	667	848	1,295	1,440	931
SG&A Exp.	110	115	136	156	134	122	123	127	147	128
Operating Profit	453	419	509	415	(4)	(82)	80	281	138	(143)
Operating Margin	43.4%	38.6%	41.2%	32.2%	-0.6%	-12.2%	9.5%	21.7%	9.6%	-15.4%
Net Profit	144	191	318	244	(170)	(121)	48	210	25	(1,133)
Net Margin	13.8%	17.6%	25.7%	19.0%	-23.1%	-18.1%	5.7%	16.2%	1.7%	-121.6%
Free Cash Flow	(96)	(62)	140	(105)	(56)	127	190	230	226	99
Income Tax	175	163	246	166	3	(48)	48	64	82	(269)

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	2,679	3,092	3,483	3,778	3,033	3,031	3,161	4,604	4,491	3,222
Cash & Equivalents	230	103	366	104	30	47	37	20	22	5
Accounts Receivable	173	181	157	148	116	98	132	191	162	154
Inventories	14	26	16	8	9	11	14	20	22	11
Total Liabilities	1,375	1,666	1,871	2,037	1,694	1,861	1,934	2,536	2,613	2,497
Accounts Payable	292	302	252	257	179	135	174	330	239	233
Long-Term Debt	366	645	930	1,067	1,000	1,010	1,010	1,319	1,473	1,517
Shareholder's Equity	1,304	1,426	1,612	1,741	1,339	1,171	1,227	2,068	1,878	726
D/E Ratio	0.28	0.45	0.58	0.61	0.75	0.86	0.82	0.64	0.78	2.09

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	5.8%	6.6%	9.7%	6.7%	-5.0%	-4.0%	1.6%	5.4%	0.5%	-29.4%
Return on Equity	12.3%	14.0%	20.9%	14.6%	-11.1%	-9.6%	4.0%	12.7%	1.3%	-87.0%
ROIC	9.6%	10.2%	13.8%	9.1%	-6.6%	-5.3%	2.2%	7.5%	0.7%	-40.5%
Shares Out.	96.4	99.1	102.1	107.3	112.0	118.3	122.1	152.8	156.6	158.9
Revenue/Share	11.31	10.91	12.07	12.00	6.71	5.76	6.93	9.10	9.22	5.90
FCF/Share	(1.04)	(0.63)	1.37	(0.98)	(0.51)	1.10	1.55	1.61	1.45	0.63

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

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