Canadian Natural Resources (CNQ)

Updated August 30th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	$58	**5 Year CAGR Estimate:**	-0.1%	**Market Cap:**	$63.7 B
Fair Value Price:	$102	**5 Year Growth Estimate:**	-15.0%	**Ex-Dividend Date:**	9/15/2022
% Fair Value:	57%	**5 Year Valuation Multiple Estimate:**	12.0%	**Dividend Payment Date:**	10/5/2022
Dividend Yield:	4.1%	**5 Year Price Target**	$45	**Years Of Dividend Growth:**	6
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Rating:**	Sell

Overview & Current Events

Canadian Natural Resources is an energy company that operates in the acquisition, exploration, development, production, marketing, and sale of crude oil, natural gas liquids (NGLs), and natural gas. The company is headquartered in Calgary, Alberta, and the common stock is cross listed on the Toronto Stock Exchange and the New York Stock Exchange, where it trades with a market capitalization of US$63.7 billion. All the figures in this report are in U.S. dollars.

In early August, Canadian Natural Resources reported (8/4/22) financial results for the second quarter of fiscal 2022. The company grew its production 6% over the prior year's quarter, with record gas production, which was 30% higher year-on-year. The company also greatly benefited from the 13-year high prices of oil and gas, which resulted from the sanctions of western countries on Russia for its invasion in Ukraine. As a result, Canadian Natural Resources nearly tripled its earnings-per-share. Given the sustained impact of the war in Ukraine on the prices of oil and gas, Canadian Natural Resources remains on track to achieve record earnings this year.

Canadian Natural Resources raised its dividend by 11% in the first quarter of 2021, by 25% in the fourth quarter of 2021 and by 28% this year. It has thus grown its dividend (in CAD) for 22 consecutive years, at a compound annual growth rate of 20%. This is an admirable accomplishment for a company that belongs to the highly cyclical energy sector. The company reiterated that its dividend is covered by cash flows even at WTI prices of $35 thanks to its low-cost reserves.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$1.47	$2.17	$3.02	$0.18	-$0.44	$0.92	$2.06	$2.40	-$0.51	$4.93	***$8.50***	***$3.77***
DPS	$0.42	$0.56	$0.78	$0.69	$0.68	$0.85	$1.00	$1.13	$1.26	$1.59	***$2.37***	***$2.55***
Shares[1]	1,092	1,087	1,092	1,095	1,101	1,223	1,191	1,184	1,183	1,185	***1,170***	***1,100***

As Canadian Natural Resources is an almost pure upstream company, its financial performance has been extremely volatile over the last decade. Given its high sensitivity to commodity prices, it is nearly impossible to make accurate forecasts. The company posted record earnings in 2021 and is on track for much greater earnings this year thanks to the 13-year high prices of oil and gas. Moreover, Canadian Natural Resources grew its proved reserves by 11% in 2019, 10% in 2020 and 6% in 2021, and thus enhanced its reserve life index to 30 years. As this figure is more than twice as much as the average life of reserves of its peers (~11 years), it is impressive and certainly bodes well for the future production growth prospects of the company. On the other hand, given the high comparison base formed by the blowout expected earnings this year, we expect a -15.0% average annual decline of earnings-per-share over the next five years.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	21.5	14.3	12.1	---	---	34.6	15.8	11.3	---	6.9	***6.8***	***12.0***
Avg. Yld.	1.3%	1.8%	2.1%	2.7%	2.5%	2.7%	3.1%	4.2%	6.3%	4.7%	***4.1%***	***5.6%***

[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.

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Canadian Natural Resources has traded at an average price-to-earnings ratio of 13.7 over the last decade if we exclude the 2015 – 2017 period, in which the stock's valuation was not meaningful due to depressed earnings. The stock is now trading at a price-to-earnings ratio of 6.8. If the company achieves our anticipated earnings-per-share of $3.77 by 2027, we expect the stock to trade around 12 times its annual earnings in that year. As a result, the stock could enjoy a 12.0% annualized gain thanks to expansion of its valuation level.

Income investors should note that while the Canadian government applies a 15% withholding tax on dividends paid to U.S. residents (including those paid by Canadian Natural Resources), this withholding tax is waived if shares are held within a retirement account like a 401(k).

Safety, Quality, Competitive Advantage, & Recession Resiliency

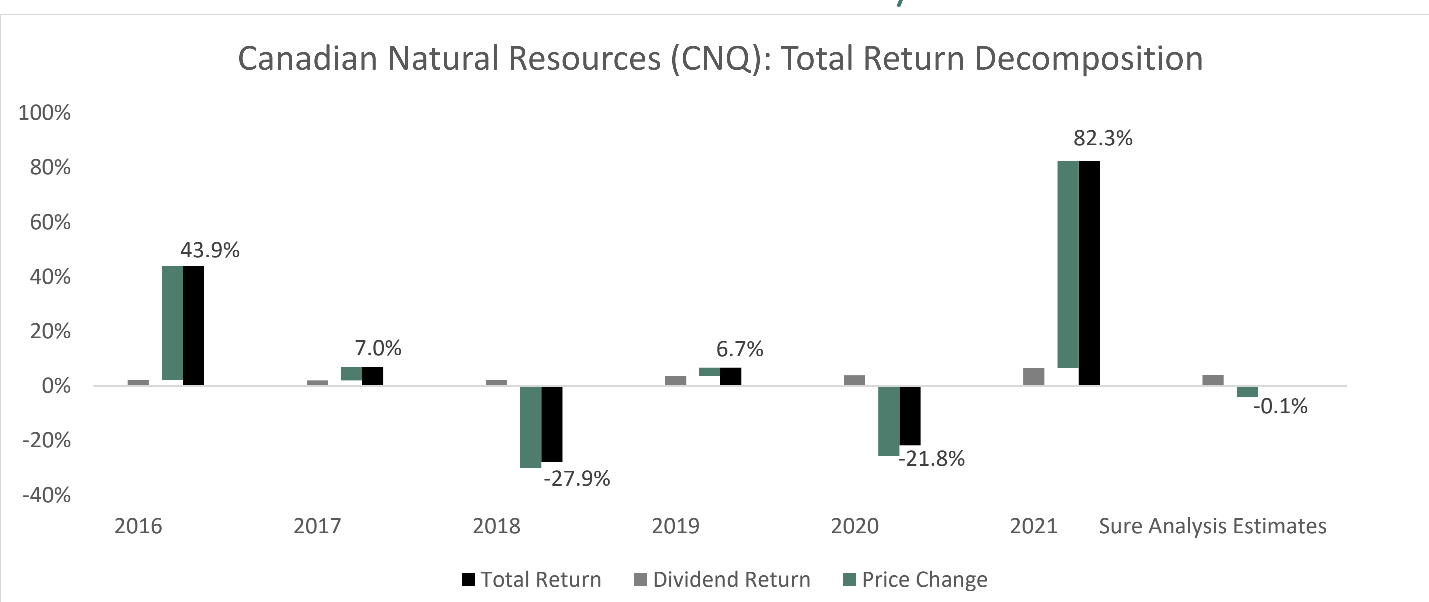
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Std. Dev.	24.8%	19.0%	27.7%	33.6%	31.6%	23.9%	48.7%	47.2%	---	32.3%	***27.9%***	***67.7%***

The competitive advantage of Canadian Natural Resources is the high quality of its assets, which have a long life, low decline rates and low production costs. However, due to the almost pure upstream nature of its business, the company is greatly affected by the prices of oil and natural gas. This is evident from its depressed earnings during the period of low commodity prices in 2015 – 2017 and the temporary -80% slump of the stock in 2020 due to the suppressed commodity prices caused by the pandemic.

Final Thoughts & Recommendation

Thanks to the sanctions of the U.S. and Europe on Russia, the prices of oil and gas have rallied to 13-year highs and the stock of Canadian Natural Resources has nearly doubled in the last 12 months. As long as the crisis in Ukraine remains in place, the company will keep thriving. However, record oil prices have always been followed by fierce downcycles. Despite the -13% decline of the stock since our last research report, in May, we expect it to offer a 5-year average annual return of only -0.1%, as its 4.1% dividend and its 12.0% valuation tailwind may be offset by a -15.0% decline of earnings. We maintain our sell rating. While the company will probably continue thriving in the upcoming quarters, investors should note its high sensitivity to commodity prices and its huge risk in the event of an unforeseen downturn.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	16,200	17,427	19,294	10,316	9,063	14,167	17,194	18,380	13,055	26,205
Gross Profit	3,261	3,694	4,969	(176)	(330)	2,278	4,023	4,784	51	8,436
Gross Margin	20.1%	21.2%	25.8%	-1.7%	-3.6%	16.1%	23.4%	26.0%	0.4%	32.2%
SG&A Exp.	56	456	392	270	529	350	138	427	231	702
Operating Profit	3,054	3,072	4,402	(581)	(966)	1,802	3,741	4,213	-332	7,587
Op. Margin	18.9%	17.6%	22.8%	-5.6%	-10.7%	12.7%	21.8%	22.9%	-2.5%	29.0%
Net Profit	1,893	2,204	3,559	(499)	(154)	1,850	1,999	4,081	-325	6,113
Net Margin	11.7%	12.6%	18.4%	-4.8%	-1.7%	13.1%	11.6%	22.2%	-2.5%	23.3%
Free Cash Flow	105	147	(2,662)	912	(261)	1,978	4,383	3,934	1,608	7,964
Income Tax	717	744	1,118	(24)	(649)	367	718	(347)	-327	1,792

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	49,235	48,606	51,858	42,715	43,499	58,741	52,539	59,805	59,033	60,128
Cash & Equivalents	37	15	22	50	13	109	74	106	144	584
Acc. Receivable	1,203	1,340	1,627	920	1,064	1,906	843	1,887	1,717	2,440
Inventories	557	594	573	378	511	711	701	882	831	1,214
Total Liabilities	24,825	24,402	26,971	22,983	24,017	33,570	29,063	33,018	33,640	31,152
Accounts Payable	467	598	486	411	441	616	572	625	523	630
Long-Term Debt	8,781	9,073	12,062	12,102	12,464	17,859	15,141	16,063	16,824	11,525
Total Equity	24,409	24,204	24,888	19,731	19,482	25,171	23,475	26,787	25,393	28,976
LTD/E Ratio	0.36	0.37	0.48	0.61	0.64	0.71	0.65	0.60	0.66	0.40

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	4.0%	4.5%	7.1%	-1.1%	-0.4%	3.6%	3.6%	7.3%	-0.5%	10.3%
Return on Equity	8.1%	9.1%	14.5%	-2.2%	-0.8%	8.3%	8.2%	16.2%	-1.2%	22.5%
ROIC	5.9%	6.6%	10.1%	-1.5%	-0.5%	4.9%	4.9%	10.0%	-0.8%	14.8%
Shares Out.	1,092	1,087	1,092	1,095	1,101	1,223	1,191	1,184	1,183	1,185
Revenue/Share	14.73	15.98	17.59	9.43	8.24	11.98	14.05	15.41	11.05	22.08
FCF/Share	0.10	0.13	(2.43)	0.83	(0.24)	1.67	3.58	3.30	1.36	6.71

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