3 Top Oil Stocks Yielding Up to 5.9%

Description

Get ready for more pain at the pump.

Some of Canada's largest cities, including Toronto and Montreal, saw prices rise more than $0.02 per litre over the weekend. In eastern Canada and British Columbia, prices have spiked to all-time highs.

Most analysts blame the steep climb on uncertainty over Iraq's oil supplies amid civil unrest. Armed militant groups have taken over several cities in the country, forcing thousands to flee the region. Others point to the U.S. economic recovery, which has been picking up steam in recent months.

Regardless of the reason, it doesn't take a rocket scientist to figure out that surging oil prices mean higher profits for energy companies. With producers gushing with cash flow, much of that money will be returned to shareholders in the form of dividends and share buybacks. For those of us trying to "Iraq-proof" our portfolios, here are three top income ideas from the oil patch.

1. Enerplus

The past five years have been tough on **Enerplus** (TSX: ERF)(NYSE: ERF).

The Canadian oil patch has been completely transformed thanks to the overhaul of Canada's tax rules, the financial crisis, and the fracking revolution. While those developments have created opportunities for some, they hurt former royalty trusts like Enerplus.

However, under the leadership of new Chief Executive Ian Dundas, Enerplus has transformed itself into a fast-growing exploration and production company. The company is building out its position in fast-growing shale plays like the Bakken and the Marcellus. That growth could be even larger than anticipated given the potential for tighter well spacing, improved fracking techniques, and new oil discoveries.

Given that the stock is trading at a 52-week high, it's apparent that investors are buying into the strategy. While investors wait for that growth to materialize, they are being paid a hearty 4.2% yield.

2. Canadian Oil Sands

Almost everything seems to be going right for **Canadian Oil Sands** (TSX: COS), the largest shareholder in the massive Syncrude Canada oil sands operation.

Thanks to to rail and pipeline capacity, the price it receives for its energy production is rising. With most of its major capital spending behind it, major project spending is expected to fall 80% to only $100 million per year by 2015. Needless to say, this combination means an enormous amount of extra cash flow. Today the stock yields 5.7%, and investors can expect more dividend hikes in the years ahead.

The only hitch in the Canadian Oil Sands bull thesis are recent reports of “unplanned maintenance” at the company’s Syncrude facility. In April, the stock was hammered after the company reported that a coker, a processing unit designed to convert oil sands bitumen into refinery-ready crude, had broken down. However, given that the Syncrude project has an estimated reserve life of 40 years, a three-month coker shutdown isn’t really a concern for the long-term investor.

3. Baytex Energy

Investors love **Baytex Energy** (TSX: BTE)(NYSE: BTE) because of the company’s growth-plus-yield business model. Over the next five years, management plans to grow oil production by 5% to 10% per year. While investors wait for this story to play out, shareholders receive a juicy 5.9% monthly dividend.

The key to building a small company capable of paying a dividend is selecting assets with very low decline rates. Baytex has amassed a significant inventory of long-term, low-cost crude oil projects, most notably in the Peace River area of northwest Alberta and the Lloydminster heavy oil region of west central Saskatchewan and east central Alberta. The company has also accumulated positions in faster-growing shale plays like the North Dakota Bakken and the south Texas Eagle Ford.

While this payout may seem high, Baytex should be easily able to fund this dividend. The company generated $1 in cash flow from operations for every $1.30 in debt. Historically, Baytex has paid out between 40% and 50% of its funds from operations.

The bottom line is that pain at the pump is creating opportunities for savvy investors. If you can stomach the volatile oil prices, this sector is an excellent addition to any income portfolio.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:ERF (Enerplus Corporation)
2. TSX:BTE (Baytex Energy Corp.)
3. TSX:ERF (Enerplus)

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