



Canadian Oil Sands Ltd. vs. Baytex Energy Corp.: Which 8% Dividend Yield Is Safe?

Description

The rout in the oil market has income investors wringing their hands as some of Canada's biggest dividends are starting to look like they might get cut.

Canadian Oil Sands Ltd. (TSX: COS) and **Baytex Energy Corp.** ([TSX: BTE](#)) (NYSE: BTE) are big companies with fat payouts. Let's look at both stocks to see if the dividends are still safe.

Canadian Oil Sands

With a dividend yield that now tops 8%, Canadian Oil Sands is attracting a lot of attention from income-hungry investors. For people who already own the stock, the 29% drop in the share price over the past three months is a bit unsettling.

Canadian Oil sands owns about 37% of the Syncrude oil sands project. The company continues to struggle with operational issues and just reduced its 2014 production guidance for the third time this year.

Third quarter year-over-year profit fell nearly 65% to \$87 million. That's on the heels of a 20% drop in Q2 earnings compared to the same time in 2013.

The only positive for investors is the impending completion of a large capital project that has been a drain on cash flow. In the Q3 earnings statement, Canadian Oil Sands said the Mildred Lake Mine train replacement is almost finished. The completion of the \$4 billion project should free up funds to provide some near-term support for the dividend.

Baytex Energy Corp.

At the current share price of \$34, Baytex's \$2.88-per-share dividend yields about 8.5%. Baytex recently increased the payout after completing its \$2.8 billion purchase of Aurora Oil and Gas Ltd.

The company primarily produces crude oil and natural gas liquids. With assets located in the Western

Canadian Sedimentary Basin, as well as the liquids-rich Eagle Ford and Williston Basin plays in the U.S., Baytex has a top-tier portfolio of properties.

The company had 51% of its WTI oil exposure hedged at \$96.45 per barrel during the third quarter, meaning the drop in crude prices should be less punitive on earnings than the market is expecting.

Baytex also has a very low dividend payout ratio. In the second quarter, the company's payout ratio was 47% before accounting for the dividend reinvestment plan. Many of Batex's shareholders take dividends in the form of new stock instead of cash. As a result, the payout ratio actually drops to 37%.

The bottom line

Canadian Oil Sands doesn't have a great track record when it comes to dividend consistency. In fact, the company tends to make dramatic cuts when times get tough, so new investors should be careful chasing the big yield right now. If oil prices continue to fall through 2015, the payout could get cut before the end of next year. The payout ratio is already approaching 90%. This means there isn't a lot of room to ride out a prolonged drop in crude prices.

I think the better bet right now is to go with Baytex given its strong hedging program and conservative payout ratio.

If oil prices stabilize at current prices, both Canadian Oil Sands and Baytex will probably maintain their payouts through next year, but that's not what the market is forecasting. If you are looking for less risk in your portfolio, you might want to check out the stocks highlighted in the following free report.

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1. TSX:BTE (Baytex Energy Corp.)

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