Should You Buy Lightstream Resources Ltd. After its Dividend Cut?

Description

It’s time to add one more energy company to the list.

On Monday, after markets closed, **Lightstream Resources Ltd.** (TSX: LTS) announced its 2015 capital program, which includes a 62.5% dividend reduction. The company also announced plans to sell all of its Bakken assets. In response, Lightstream’s shares fell by more than 7%, even though the Canadian energy sector saw big gains during the day.

So is now the time to take advantage of a discounted share price? Below we take a look.

We could all see this coming

Lightstream’s dividend cut should have come as no surprise. The company was already under financial pressure even before oil’s recent collapse, with nearly $1.5 billion of debt (even after selling a big chunk of assets to **Crescent Point Energy Corp.**). And now that oil has declined by 50% since its June peak, the dividend was clearly unaffordable. Investors seemed to understand this perfectly – the stock closed Monday with a dividend yield of 34%.

Yet the shares still fell

This kind of thing has happened a few times in Canada’s energy sector recently. And it makes little sense. After all, if everyone knows a dividend cut is coming, why does the share price tank so much when the payout is actually reduced?

Quite simply, there are a large number of investors that hold onto these investments because they’re looking for a high yield. Others simply don’t want to dump the stock at a loss. These investors seem to bail en masse when the dividend cut arrives, even if everyone else can see it coming.

So is now the time to buy Lightstream?

To put this succinctly, the answer is no.

First of all, Lightstream is not out of the woods yet. It still has to deal with its $1.4 billion debt load, a massive amount for a company valued at less than $300 million by the market.

In order to deal with this burden, the company hopes to sell all of its assets in the Bakken “at an appropriate valuation.” Of course, the company will be selling these assets right into a massive buyer’s market, and have much difficulty getting a fair price. This is not an enviable position to be in.

Making matters worse, Lightstream still pays out a pretty fat dividend (the company now yields 13.7%). So there’s still a possibility of yet more dividend cuts – it depends on what happens to the oil price. And we’ve all seen what happens to share prices when dividends get cut.

Any alternatives?

Here’s a good rule of thumb: Don’t buy a Canadian energy stock if it yields more than 5%. These companies are all struggling mightily, and more dividend cuts could be on the way.

CATEGORY

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