Could Baytex Energy Corp. Double in 2015?

Description

Back in June, **Baytex Energy Corp.** (TSX: BTE)(NYSE: BTE) closed its $2.8 billion acquisition of Aurora Oil and Gas Limited, and raised the dividend by 9% from $2.64 to $2.88 per share.

At the time, the stock was trading above $47.00 per share, and Aurora's Eagle Ford shale assets were expected to drive revenue and free cash flow much higher for years.

Six months later, the world looks a lot different. No one could have imagined back in June that Baytex would slash its dividend in December by nearly 60% and reduce 2015 spending by 30% in order to preserve capital. Shareholders watched in horror as the stock dropped like a rock, falling below $15 per share.

Baytex now expects to spend between $575 million and $650 million next year. Roughly 75% of the capital will be invested in the Eagle Ford assets.

During the past two weeks, Baytex has enjoyed a 30% bounce and now trades at about $20 per share. This is little consolation for investors who bought the stock in the summer, but new investors looking to add an oil stock to their portfolios are wondering if the current 6% dividend is safe.

Let's take a look at three reasons why Baytex Energy could continue to rebound in 2015.

1. Higher oil prices

West Texas Intermediate (WTI) oil is trading below $60 per barrel right now. That is an ugly number for many North American producers, especially those with high costs in the shale plays.

The game of chicken being played out between OPEC, Russia, and North American producers is likely to end sooner than later, and oil prices should drift higher through 2015.

Arabian Gulf producers need high oil prices to cover the cost of generous social programs. According to a former advisor, Saudi Arabia is likely basing its 2015 budget on an average oil price of about $80 per barrel. On December 21, Saudi Arabia's oil minister said oil prices will rise as high-cost production slows and global demand increases.

Any sustained move in the oil price back above $80 per barrel should send the shares of Baytex significantly higher, given the size of the selloff.

2. Strong production growth

Baytex reported a 41% year-over-year production increase for the third quarter. The company's Eagle Ford assets are producing well, and should continue to deliver solid output in 2015.

3. Hedging

Baytex has done a good job of hedging its production. For its Q4 WTI exposure, the company said it was 51% hedged at a weighted average price of $96.45 per barrel (bbl). More importantly, Baytex said it had 37% of its WTI exposure hedged at $94.79/bbl for the first six months of 2015, and roughly 11% hedged at $94.23/bbl for the second half of next year.

Given the size of the dividend cut and reduced 2015 capital expenditure announced on December 10, it appears Baytex is being extremely cautious, or is expecting very low oil prices to continue right through next year. In the Q3 earnings statement released at the end of October, Baytex said it expected to generate enough funds from operations to cover both the $2.88 dividend and capital requirements through 2015 assuming average WTI prices of $80 per barrel.

Should you buy?

If oil rebounds and stabilizes above $80 before next summer, there is good reason to believe that Baytex investors could see an increase in the dividend. If that happens, Baytex might regain the $40 per share mark by the end of 2015.

The oil market remains volatile and there are still risks to dividend payouts if crude prices don't rebound. If you are looking for a safer income alternative, the following report analyzes one top stock that has a consistent track record of stability and dividend growth.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)

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