Can Investors Count on Crescent Point Energy Corp.'s 8.5% Dividend Yield?

Description

Over the last six months, dozens of Canada's oil producers cut their dividends.

One notable exception is **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) and its current 8.5% yield. When oil slid beneath $50 per barrel, pundits everywhere thought the company would be the next to chop its payout, especially considering how generous it is. Sure, management did have the advantage of hedging approximately 50% of its 2015 oil production at prices north of $90 per barrel, but it still hurts to sell the other half at $50 per barrel.

Plus, the fact is that the company hasn't had the free cash flow to support the dividend for years, even during times when oil traded above $100 per barrel. And that's even after offering investors a 5% discount to take their dividends in the form of additional shares instead of cold, hard cash.

What does 2015 look like? Will the company be able to continue paying shareholders $0.23 per share each month? Let's take a closer look.

Cash from operations

Many of Canada's large oil producers gave investors a detailed prediction of what expected results might be for 2015. Crescent Point's numbers were a little light, so we'll have to fill in a few ourselves.

In the fourth quarter of 2014 the company averaged $65 per barrel of oil sold, partially weighed down by its natural gas production. Considering the hedging in place, I think it's safe to assume it can maintain that average price in 2015. Production was around 150,000 barrels per day.

The company generated $572 million in funds flow in the quarter, which we'll round down a little to $2 billion for the year. We want to be conservative when doing stress tests like this one. Included in the 2014 fourth-quarter numbers was the company's projected capital expenditures for 2015, which came in at $1.45 billion.

That leaves a projected free cash flow of $550 million, or about $1.20 per share. Compare that with the dividend of $2.76 per share, and we have a problem. Even with the hedging program in place, Crescent Point continues to be in a position where it can't afford the dividend.

The bright side

The good news for investors is this isn't a big deal, at least for the rest of 2015.

Crescent Point has approximately 450 million shares outstanding, and 30% of shareholders elect to take advantage of the 5% discount to get more shares instead of a cash dividend. Which means that the company will have to pay out $870 million in cash in 2015, give or take a few bucks.

Remember, free cash flow is $550 million, which means the shortfall is more like $320 million. We're still talking about a gap of $0.71 per share, but it's a whole lot better than the $1.56 per share gap.

For a company the size of Crescent Point, borrowing $320 million to pay the dividend isn't the end of the world. It has $2.3 billion available on its credit line, after negotiating with lenders to give it an additional $1 billion in borrowing power. Based on that, I'm pretty confident in assuming that the 2015 dividend is safe.

But here's where it gets tricky. It's generally not a good idea to count on any dividend in the long-term from a company that has to borrow to make the payments. As we've all seen countless times, credit has a habit of drying up right when a company needs it most. I'm not saying that's about to happen to Crescent Point, but the fact remains that a borrowed dividend is far less secure than one covered by free cash flow.

If oil recovers by the end of the year and the company can average $75 or $80 per barrel of crude produced, Crescent Point should have a truly sustainable dividend for the first time in years. But until it happens investors have to be concerned about the viability of the payout. Crescent Point is just too dependent on oil's recovery to make it a really dependable dividend.

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