



Freehold Royalties Ltd: Is it Time to Get Back into Oil Stocks?

Description

The U.S. Energy Information Administration (IEA) recently reported that world demand for oil will rise more than expected in 2015, but it also raised its forecast for supply growth this year. However, the demand forecast was raised by 280,000 barrels per day, while the supply estimate was raised by 195,000 barrels per day.

Even more recently, U.S. gasoline demand in the week of June 19 was at the highest level for the period since 1991, and there was a larger than expected fall in U.S. crude inventories. So, demand expectations have been too low and supply expectations may have been too high.

As an investor, it makes me think that if the market has become overly bearish on oil to the point where it is underestimating demand and overestimating supply, this would mean the price of oil will go higher than current expectations. And this would translate into the stocks going higher than current expectations.

Freehold Royalties Ltd. ([TSX:FRU](#)) is a company that, in my view, is a good way for investors to increase their weighting in the energy sector. The company has a stable business model and, with a dividend yield of 6.54%, Freehold Royalties is a low-risk way for investors to add to their energy weighting.

The company recently acquired two royalty packages from **Penn West Petroleum Ltd.** for \$330 million, which was funded through an equity issue and is expected to provide operating income accretion of 6% in 2015.

Penn West Petroleum has been struggling with debt and needed to get its hands on some cash quickly in order to meet its debt covenants, and Freehold was ready to take advantage of this situation and add high-quality assets to its portfolio of royalty-producing properties. The acquisition has increased the percentage of revenue that comes from royalties to 83% from 79%, and has also increased the company's weighting towards oil. Oil volumes now represent approximately 65% of total volumes.

Freehold's stock has a one-year return of -40%, and is trading at relatively cheap valuations. The company has beat expectations in the last two quarters, has strong margins and a strong ROE of

almost 20%. The one problem with this company is that the payout ratio is high, but with a debt to capitalization of 32%, there is room on the balance sheet.

Another tidbit of information that is encouraging is the fact that there has been some insider buying as of late, with Director Martin Romanow buying 15,000 shares and Director Joseph Bugeaud buying 12,000 shares.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

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1. Editor's Choice

TICKERS GLOBAL

1. TSX:FRU (Freehold Royalties Ltd.)

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