Investors React Favourably to Freehold Royalties Ltd.'s Dividend Cut

Description

Freehold Royalties Ltd. (TSX:FRU) announced a 22% cut to its dividend from $0.09 per share to $0.07 per share. This follows the January dividend cut from $0.14 to $0.09. So, why are investors happy?

Well, first of all, they are happy because oil prices are up today as the Energy Information Agency reported that crude inventories are falling by 2.1 million barrels after many reports of inventories building.

But they are also happy because a dividend cut was widely expected, and it takes the pressure off the company. It was the prudent thing to do as it preserves cash and protects the balance sheet. The energy market is cyclical, and just as dividends are increased as oil prices rise, sometimes they need to be decreased when oil prices fall. This is just the nature of a company in a cyclical business.

So, we are now clearly at the low end of the cycle. And what better time to buy a stock when it is a good quality company that is in an industry that is struggling at the moment?

On this note, while many analysts have given the stock a hold recommendation, there are key attributes of the company that make it a good candidate to buy because once the oil market settles and rebalances, it should emerge stronger than before.

Here are the reasons why I think Freehold Royalties will survive and thrive in the long term.

Royalty-focused production

This means a low-risk business model as the company does not pay any of the costs. Freehold's production is currently 73% royalty production, and royalties make up 83% of operating income.

Opportunistic acquirer

Acquiring in a market downturn sets Freehold up to emerge from the downturn even stronger. Freehold announced over $400 million in transactions in 2015, such as Anderson Energy, which added 350 boe/d of low-decline working interest production, and the Penn West asset acquisition, a $321 million royalty acquisition from Penn West, adding 1,400 boe/d of royalty production with $29 million in 2015 annualized CF at US $60/bbl.

Diversified production

Royalty production is from over 30,000 wells and over 200 operators. The top payer represents 7% of total royalty revenue.

While Freehold will not make as many acquisitions in the second half of this year, the company will continue to accumulate royalty production from quality assets, have attractive returns and an acceptable risk profile, and have a long economic life.

And P.S., the dividend yield is still over 7%.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. TSX:FRU (Freehold Royalties Ltd.)

Category

1. Dividend Stocks
2. Energy Stocks
3. Investing

Date
2025/08/27
Date Created
2015/09/17
Author
karenjennifer