Baytex Energy Corp. Buys Itself Some Breathing Room

Description

The continued weakness of oil prices has shone a spotlight on the balance sheets of small oil and gas companies such as **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE). Many of these companies borrowed heavily to fund growth when oil was in the triple digits, leaving them with a lot of leverage now that oil is much weaker. As such, these companies have had to work overtime to address their balance sheet concerns in order to steer clear of potential bankruptcy filings.

That's something Baytex recently did; it took another step away from the ledge after amending its credit facility.

What Baytex did

Baytex announced last week that it and its banks had agreed to a number of amendments to its bank credit facilities that will increase the company's financial flexibility. These amendments included reducing its credit facilities from US$810 million to US$575 million, granting its banking syndicate first priority security over its assets and restructuring its financial covenants.

While the US$240 million reduction did wipe away some of the company's liquidity, it will actually save the company $8 million per year from lower interest expenses and standby fees. Further, with only 32% of the revised amount borrowed, it still has ample liquidity.

Easing concerns of a breach

More important than having a little extra liquidity was the easing of Baytex's financial covenants. These covenants, if breached, could have put the company in default, which could have then triggered early repayment clauses. Now the company can breathe much easier because it has a lot more room between its current leverage metrics and its amended financial covenants.

In fact, with a senior secured debt-to-bank EBITDA ratio that stood at 0.43 times as of the end of last year, Baytex has a lot of room before it would bump up against its revised five times ratio, which has been set for the next two years.

That’s a lot more room that Canadian peer **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE) has right now. As of the end of last year, Penn West warned that its senior debt-to-EBITDA stood at 4.6 times, which was dangerously close to its five times covenant. Worse yet, given its oil price and earnings projections, Penn West warned that it “anticipate[s] that we will not be in compliance with our existing financial covenants by the end of the second quarter of 2016.”

Penn West was exploring several options to address its default risk, including engaging with its banks to amend its financial covenants as well as selling additional non-core assets. It has recently made progress on the asset sales, selling $230 million in assets, and it made the tough decision to part with its core Slave Point assets. It was a sale the company deemed necessary to improve its financial flexibility and credit metrics.

Given that Baytex is well under its limits, it doesn’t need to sell assets to stay afloat. Instead, the company remains focused on living within its cash flow, so it can maintain its relatively solid financial footing.

Investor takeaway

With its credit facility amended, Baytex Energy doesn’t have to worry about another big drop in oil prices causing a covenant breach. That puts it in a much better position than peers like Penn West to weather the current storm. Having said that, Baytex still faces a number of headwinds, including the fact that a growing portion of its production isn’t even profitable at current oil prices, suggesting that it’s not out of the woods just yet.

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1. TSX:BTE (Baytex Energy Corp.)

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