



Is Baytex Energy Corp. Set to Drop Again?

Description

Shares of **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) are up over 130% in the past 90 days, stemming from newfound optimism in the oil sector. Despite the recent fervor, there is one metric indicating that there could be trouble ahead.

Credit versus equity

Before the recent rebound, Baytex shares had fallen over 95%. While the collapse in oil started the panic, bankruptcy fears nearly sent the stock to zero. Net debt is still higher than the company's entire market cap and **Moody's Corporation** downgraded Baytex this year to below investment grade, giving it a negative outlook.

The company has less than \$600 million left in undrawn credit facilities (which mature in 2019) and is burning through piles of cash every quarter.

Recently, Baytex received some good news. This month, the company announced amendments to its bank credit facilities and a restructuring of its financial covenants. The moves should keep Baytex financially solvent over the new few quarters.

"With these amendments to our bank credit facilities, we expect to have adequate liquidity and financial flexibility to execute our business plan. In addition, we are well positioned to benefit from an oil price recovery as our three core plays provide some of the strongest capital efficiencies in North America," the company said.

Despite the latest pop in shares signaling renewed optimism, the company's bondholders don't share the same level of enthusiasm. Since November, the company's bonds have sifted downward from the mid-\$80s to below \$70. Just a few weeks ago they were yielding over 10%.

Should you be concerned?

There are a few reasons why the bonds are likely still depressed. First, the credit downgrade of its senior unsecured notes stemmed from Baytex's amended deal with its banks, giving its lenders

security over the company's assets. Second, ratings downgrades have a real impact on the short-term cost of financing.

Most companies that fall below investment grade see their bonds forcibly sold off by mutual funds that are mandated to only hold investment-grade securities. This also creates lower demand for future debt rounds. So Baytex's struggles seem to beget even more troubles.

If oil continues rising, however, none of this matters that much. The company's hedging program also gives is a nice boost this year if the market is slow to rebalance. About 80% of 2016 oil production is hedged through a variety of contracts. In all, the hedges give Baytex a boost in profitability with prices under \$50 a barrel.

Currently, the company has an all-in breakeven of about \$40-45 a barrel, so if the latest oil rebound is sustained, long-term investors shouldn't fret too much about Baytex's issues in the credit markets.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)

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