Baytex Energy Corp.: If You Don’t Buy Now, You’ll Be Kicking Yourself Later

Description

Allow me to make a bold statement: I believe the bottom on the price of crude oil is behind us.

Sure, crude could easily dip below $40 per barrel again. It could even dip below $35. Or it might linger right around the $40 level for months before heading higher. I really don’t know. If there’s one lesson I’ve learned from the last 18 months in the energy market, it’s that trying to guess short-term movements in the price of volatile commodities is a sucker’s game.

So I can’t tell you where I think crude is going in a week, a month, or even a year. I’m fairly confident crude will be higher a year from now, but I could easily be wrong.

If you expand the prediction to five years out, my confidence increases. I’m just about 100% confident that crude will be higher in 2021 than it is now. Worldwide demand continues to increase, while supply will head lower. And since this downturn will affect the industry for years, I doubt production will come roaring back when prices recover. Producers will dip their toes back in rather than doing a cannonball from the high diving board.

What investors have to do is figure out which energy companies are poised to survive the downturn. Many of these stocks are already up handily from lows, as astute investors recognize the worst is behind us. As long as a company has a relatively low cost of production and a solid balance sheet, it should not only survive, but it represents a good investment opportunity.

I believe such an opportunity exists today with **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE). Here’s why I think shares of this beleaguered energy producer will be much higher when crude inevitably recovers.

Making smart moves

Baytex has been making smart moves to ensure its survival.

Most recently, the company shuttered its heavy oil production in northern Alberta because it simply wasn’t economical. Breakeven costs were approximately $45 per barrel. Oil was hovering around $38 at the beginning of April, making the decision easy.

Things look more optimistic for the company's production in the Eagle Ford formation in Texas. Breakeven costs are $32 per barrel there, which ensures enough cash flow for the company to pay its bills and spend a little bit on expanding in the area.

Baytex has also been hedging, locking in higher average prices for much of its 2016 oil production. Additionally, it has locked in prices of close to $3.00 per GJ for 41% of its natural gas production.

And finally, Baytex doesn't have any long-term debt maturing until 2021. This gives the company ample time to wait for oil to recover before being forced to pay down its $1.85 billion in debt.

Levered to oil

Like many of its peers, Baytex has turned into a levered play on the price of oil. If crude heads higher, so do Baytex shares. If crude declines, the opposite happens.

In late January, when crude was below $30 per barrel and everybody was worried about the possibility of prices dropping even further, Baytex shares dipped below $2 each on the Toronto Stock Exchange.

Just a few months later, things are very different. Crude is comfortably over $40 per barrel, and Baytex shares are at $6.20 each, and that's even after a 6% decline in trading on Monday morning. Shares more than tripled in just three months.

If crude continues to recover, Baytex still has huge upside. Back in the early part of 2015–when crude traded at more than $60 per barrel–Baytex shares traded hands for more than $20 each. If we see a similar valuation when crude returns to $60, Baytex shares will triple again. Not bad on a 33% move in the price of crude.

Crude will eventually recover. And when it does, Baytex shares should soar. Do you really want to be on the sidelines if that happens?

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1. TSX:BTE (Baytex Energy Corp.)

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