



Baytex Energy Corp.: This Turnaround Still Has Plenty of Upside Potential

Description

When oil cratered to below \$30 per barrel, it looked as though every producer was on a one-way trip to bankruptcy.

Oh, what a difference a few months makes. Oil staged a massive recovery from the lows, rallying all the way up to \$50 per barrel. That might not seem like much compared to prices we've seen for the commodity in recent history, but it's huge for energy producers with a cost per barrel in the \$35-45 range. These companies have improved from being nearly insolvent to just struggling.

Naturally, this move has been very good for the share prices of many of Canada's most beleaguered energy producers. Perhaps the biggest beneficiary has been **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE).

Back in January, when oil was selling at a level far below Baytex's breakeven of approximately \$35 per barrel, shares of the energy producer fell all the way down to \$1.94 on the Toronto Stock Exchange.

Investors who were brave enough to get in then have been treated to one heck of a ride. As I type this, Baytex shares have surpassed \$8. This represents a return of more than 300% in less than six months. That's the kind of result that can really supercharge a whole portfolio.

After such a big move, investors are right to be worried. It's only natural to expect a pullback. If oil declines from today's levels, it's only natural Baytex shares would tumble in response.

Over the short term, I have no idea where Baytex shares will go. If you're like me and believe oil will eventually recover to more normalized levels of between \$70 and \$90 per barrel, then there's a high probability Baytex shares will be much higher.

Here's why.

Low-cost operations

Like many of its peers, Baytex has been aggressively cutting drilling costs. This has pushed breakeven

costs down to \$32 per barrel in the Eagle Ford formation in Texas. Naturally, Baytex is focusing most of its 2016 capital budget in the area.

Production is expected to be between 68,000 and 72,000 barrels of energy equivalent per day in 2016, split between oil and natural gas. That's down a bit compared to the 81,000 barrels per day it produced in 2015, but not as much as some of its peers.

This low-cost production is good news no matter what the price of crude does. If crude recovers back to \$60 per barrel, then Baytex is comfortably profitable. And if it sinks back down to \$40, Baytex is well equipped to deal with that, too.

No debt issues

One of the troubles affecting Baytex's peers is looming debt obligations. These companies are being forced to sell good assets at fire-sale prices just to pay the debt.

Baytex doesn't have such problems. Yes, the company does have quite a bit of debt—the total owing sat at \$1.8 billion at the end of March—but none of it is due until 2021. At this point, it doesn't appear that Baytex will need any additional debt because it's completely self-funding. But if it does, it still has \$450 million in unutilized debt capacity.

How much upside?

Back in early 2015, Baytex shares bounced between \$20 and \$25 each on the Toronto Stock Exchange. Oil traded for approximately \$60 per barrel.

Much has changed in a year, of course. In the spring of 2015, investors thought crude would recover to \$80 or \$100 per barrel pretty quickly. These days the mood has soured. There are plenty of pundits saying \$80 oil is nothing but a pipe dream.

For every \$10 oil has moved, Baytex shares have roughly doubled. From \$30 to \$40 Baytex moved from \$2 to \$4 per share. From \$40 to \$50 Baytex shares doubled again to \$8. Keeping in mind that we've already seen shares trade at \$20 per share while oil sat at \$60 per barrel, I don't think a target price of \$15-16 per Baytex share is unreasonable if oil goes up another \$10.

Thus, even after a 300% move from the bottom, I still think Baytex shares have plenty of upside—provided oil cooperates. If you're a believer in crude, it's still not too late to jump aboard the Baytex train.

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1. TSX:BTE (Baytex Energy Corp.)

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Date

2025/09/11

Date Created

2016/06/08

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