



## The 2 Best Ways to Play the Next Leg up in the Oil Rally

### Description

After recovering nearly 7% post-Brexit to nearly US\$50, WTI prices are once again plunging on global fears related to the Brexit and a strengthening U.S. dollar. With oil prices trading in a tight range below US\$50 for most of the last month, it is likely that oil prices are either due for an extended pause or a further correction below US\$45 per barrel before resuming their uptrend.

This is due to a few reasons. Firstly, Brexit fears will help support the U.S. dollar going forward as central banks in both the U.K. and Europe look to ease monetary policy. Japan should also pursue further easing, which will weaken the yen. These factors combined with the United States's relative economic strength should support the U.S. dollar and weigh on oil prices.

Secondly, returning supply from Canada and Nigeria—outages that helped propel the latest rally—will continue to weigh on prices, as will the prospect of returning U.S. production (rig counts are rising once again, which is a precursor to production). What is almost certain though is that any pullback in oil prices will be temporary, making this a perfect opportunity for investors to take new positions in oil stocks.

The facts are clear—most U.S. producers need about US\$60 per barrel oil to keep U.S. production flat, and with demand growth coming in at 1.4 million barrels per day this year and expected to be strong till 2020, U.S. production will need to rise substantially as the key global producer.

With global investments in oil declining for two consecutive years (the first time this has ever happened), the potential for price spikes is high in the coming years as demand growth remains steady and the global supply network remains impaired.

Investors looking to jump on this trend can achieve a good balance with these two names

### Baytex Energy Corp.

**Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) is the highest-risk name of these two companies, but it also has some of the highest upside if oil prices rise. Baytex has significantly higher debt than its peers (a debt to cash flow of 6.9 this year, according to **Bank of Nova Scotia** compared to 4.6 for its peer

group) due to its large acquisition of Aurora in 2014 right before oil prices plunged.

Baytex will require higher oil prices to begin improving this ratio. Currently, the company has suspended drilling new heavy oil wells in Canada (which was previously a major component of the company's budget), and with Baytex not looking to add to its debt levels, it will likely only be drilling its lower breakeven Eagle Ford light oil assets in 2016.

Since Baytex is constrained to spending only its cash flow, rising oil prices will offer substantial upside since the company will be able to resume growth in all of its asset bases, which will lead to an improvement in the company's debt ratios and improvement in the stock's valuation compared to its peers.

### **Crescent Point Energy Corp.**

**Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) is much lower risk option than Baytex. It's a best-in-class North American operator according to most measures. Thanks to Crescent Point's high-quality asset base (Crescent Point's plays rank first, second, and third out of 20 North American plays in terms of how long it takes to recover costs to drill and complete wells), it has the highest cash netbacks in the industry.

Crescent Point has not had to cut production and is expecting flat production in 2016 and 2017 with considerable upside possible if prices rise thanks to its continually improving capital efficiency.

Crescent Point has been using water-flooding technology to reduce the rate at which its wells decline in production over time, which has the effect of increasing the total amount of oil recovered by over three times. Since water-flooding is fairly inexpensive, Crescent Point can bring in more barrels for less capital.

The end result is that Crescent Point estimates that a fairly small amount of capital (\$50 or \$100 million on top of its current \$950 million budget) could easily boost its estimated 2016 production from 165,000 bpd to 170,000 bpd.

### **CATEGORY**

1. Energy Stocks
2. Investing

### **POST TAG**

1. Editor's Choice

### **TICKERS GLOBAL**

1. NYSE:VRN (Veren)
2. TSX:BTE (Baytex Energy Corp.)
3. TSX:VRN (Veren Inc.)

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