



Should You Own Encana Corporation or Baytex Energy Corp.?

Description

Oil companies are rallying after the recent pullback, and investors are wondering which names are the most attractive right now.

Let's take a look at **Encana Corporation** (TSX:ECA)(NYSE:ECA) and **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) to see if one is a smart pick.

Encana

Encana has the dubious reputation of being the energy company that bet big on the expected movement in energy prices and got it wrong—twice.

After the financial crisis Encana decided to focus on natural gas and dumped all of its oil and refining assets into a new company called **Cenovus Energy**.

As we all know, WTI oil subsequently rode a wave of global stimulus to well above US\$100 per barrel. Natural gas went the other way, plunging on a massive surplus caused by the North American shale gas boom.

Investors weren't overly impressed, and Encana switched up its leadership team, hoping for better stewardship.

The new group decided to reverse course and started selling gas properties to fund a buying binge on oil assets.

That hasn't panned out so well either as the company closed two massive oil deals at what turned out to be the top of the oil market.

As oil prices tanked, the debt taken on to pay for the new properties became unsustainable, and Encana has pretty much been in survival mode ever since.

Management has done a good job of finding buyers for more of the gas properties, and the debt level

has come down as a result, but at US\$5.69 billion, the debt is still a concern.

Free cash flow was negative US\$209 million for the first six months of 2016, so Encana is still burning through lots of cash.

At the time of writing, Encana has a market capitalization of US\$8.6 billion.

Baytex

Baytex also got itself into trouble by betting big on oil assets at the wrong time, spending \$2.8 billion on properties in the coveted Eagle Ford play just as oil was about to roll over.

As with Encana, the debt load quickly became a problem and Baytex had to scramble to keep itself afloat. The company slashed spending, suspended the dividend, and renegotiated terms with lenders to buy some time.

When WTI oil plunged below US\$30 back in January, investors pretty much threw in the towel and Baytex dropped below \$2 per share. Just 18 months earlier the stock was \$48.

Cuts to the capital plan are taking a toll on production. Output fell 7% in Q2 2016 compared with the previous year, and funds from operations (FFO) came in at just \$81.3 million in the quarter, down nearly 50% from Q2 2015.

Long-term debt is \$1.54 billion and the company has used CAD\$347 million of its US\$575 million (about CAD\$735 million) in available credit.

Baytex has a market capitalization of \$1.5 billion.

Should you buy?

These stocks will continue to rally as long as oil trends higher, but the downside is substantial in both names if oil decides to repeat its plunge through the end of the year.

As such, I wouldn't buy either stock. The oil market is still too volatile.

If you are convinced you want to own one, Encana can probably survive a bit longer in the event of another downturn, but at nearly \$13 per share, this stock is no longer on sale, and a return to the low of \$4 is possible if oil goes the wrong way.

The only reason to buy Baytex would be on the hope of a takeover premium, but that's not exactly a great investing strategy.

CATEGORY

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TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)

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