



Baytex Energy Corp.: Look Out Below?

Description

Baytex Energy Corp. ([TSX:BTE](#))(NYSE:BTE) enjoyed a nice surge earlier this year, but the rally has run out of steam, and more pain could be on the way.

Let's take a look at the current situation to see why it might be a good idea to stay on the sidelines.

Tough times

Baytex dropped below \$2 per share in January this year as investors began to accept the fact that the company could go bust. That's a far cry from the party atmosphere that surrounded the stock back in the summer of 2014 when the shares traded for \$48.

What happened?

Baytex loaded up on debt to make an expensive acquisition at the top of the market. As WTI oil plunged, the company was forced to cut expenses and hope for higher prices. As soon as oil dropped below US\$30 per barrel earlier this year, investors figured Baytex was pretty much toast.

Oil subsequently rallied back to US\$50 per barrel through the spring, and the stock briefly hit \$9 per share.

Now oil is falling again, and the stock is already back down to \$5.

Where do things go from here?

Baytex reported Q2 funds from operations (FFO) of \$81.3 million on production of 70,031 barrels of oil equivalent per day (boe/d). That's down from FFO of \$158 million in the same period last year on production of about 85,000 boe/d.

Lower realized prices on falling output is a bad situation for an oil company.

Producers with strong balance sheets can ramp up spending on the low-hanging fruit in their portfolios to help offset weak prices, but Baytex is somewhat handcuffed by its debt obligations and limited

access to capital, so it can't spend any more to replace its production.

How bad is it?

Baytex finished Q2 with net debt of \$1.94 billion. That's a lot for a business with a market capitalization of just \$1 billion.

The company had its credit lines reduced as part of a renegotiation with lenders earlier this year, so Baytex only has access to US\$575 million (CAD\$760 million). A total of CAD\$347 million of the available funds had already been drawn at the end of the second quarter.

Guidance

Weak oil prices continue to put a pinch on development. Baytex cut its active drilling rigs in half from Q1 to Q2, and the company only had three rigs running on its properties at the time the Q2 report was released. As a result, full-year production guidance has been reduced from 68,000-72,000 boe/d to 67,000-69,000 boe/d.

To their credit, management has done a good job of focusing capital on the top assets and is keeping spending in line with FFO. Baytex generated FFO of \$127 million in the first six months of the year and spent \$117 million on capital programs.

Outlook

Oil prices continue to retreat. At the time of writing, WTI oil is back below US\$43 per barrel, and the trend in the near term appears to be down.

Support in recent months has come on the back of rumours that Saudi Arabia, Iran, and Russia will come to a production-freeze agreement. Pundits think the odds of a deal being reached are pretty slim, and most analysts are skeptical that any of the parties would actually honour the pact.

As such, the global oil glut is probably going to be with us for a while, and that doesn't bode well for oil prices.

Should you buy Baytex?

At this point, investors should probably avoid the stock. It could easily retest the January low if oil prices plunge in the coming months.

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