



The Unusual Way I'm Betting on Oil's Recovery

Description

Like many investors, I'm convinced the price of oil is going to head much higher at some point in the future. It's only a matter of time.

No matter how hard we try to diversify, the world still runs on oil. Each year, despite thousands of electric cars hitting the streets, the number of gas-powered vehicles continues to increase, primarily because of growth in the developing world.

There's also the possibility of a real supply crunch hitting the market. While the sector has stabilized, there's still a slow decrease in the number of rigs drilling. Eventually this will lead to lower production. With prices so low, the logical thing to do is to pack up and wait for better times.

And yet, despite my confidence and the confidence of millions of other investors, oil stubbornly sits under \$50 per barrel and looks poised to stay there for weeks, if not months.

This makes investing in an oil recovery tricky. Most energy companies will be in rough shape if crude stays at this level. Many are levered to the hilt, only surviving because of concessions made by lenders.

Take **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) as an example. The company's debt situation looks precarious on the surface. It owes nearly \$1.9 billion to creditors while only having a market cap of \$1.2 billion. It was even forced to ask its creditors to relax covenants that may have led to a technical default on its debt.

Baytex is actually in pretty good shape, since a vast majority of that debt doesn't come due until 2021. It has time to wait out the storm, in other words. That's right, a company that owes \$1.9 billion is actually doing well.

Penn West Petroleum Ltd. (TSX:PWT)(NYSE:PWE) is another example. The company only narrowly avoided bankruptcy by selling assets over the last year, including some \$1 billion worth of land in Saskatchewan that was previously identified as a core asset. In other words, the company was forced to sell something it didn't really want to get rid of and at the bottom of the market too.

Both Baytex and Penn West have performed quite well; both are up some 200% from their bottoms. If crude shoots higher, they'll continue to do well. If not, they'll still likely both survive, but the situation won't be great.

How I'm playing the market

If I believe oil is going to head higher at some point, why don't I just invest in a high-beta oil stock and be done with it?

The answer is simple. Instead of investing in an unpredictable commodity, I'd rather invest in more stable businesses that have exposure to crude oil.

Dream Office Real Estate Investment Trst ([TSX:D.UN](#)) is a great example. Approximately 30% of the company's assets are in Alberta, which has been reason enough for most investors to sell their shares and never look back.

Dream shares trade hands at just over \$17 each. Net asset value is more than \$23 per share. And just a year ago, before management wrote off value of the Alberta assets by more than 60%, the net asset value was \$32 per share. In other words, there's value there.

In its most recent quarter, Dream reported occupancy in Calgary of about 85%, although rents have dropped around 25%. Both those numbers could very well turn worse. But the Calgary market will come back. It's just a matter of time.

In the meantime, Dream is paying me a dividend of 12.5 cents per share each month, which works out to an 8.8% yield. The payout is safe too, coming in at less than 60% of funds from operations thus far in 2016. There's plenty of wiggle room if Alberta continues to be weak.

The bottom line

See the difference between Dream and Penn West or Baytex? The latter two names may represent better capital-gains potential, but Dream allows me to get exposure to Alberta's recovery, while the majority of its assets are in more stable markets like Toronto. It also allows me to get paid a very generous yield while I wait.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)
2. TSX:D.UN (Dream Office Real Estate Investment Trust)

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