



Is Freehold Royalties Ltd. About to Increase its Dividend Yet Again?

Description

Freehold Royalties Ltd. ([TSX:FRU](#)) announced better than expected first-quarter results, reflecting increasing activity and a higher commodity price deck versus a year ago.

Production increased 7%, the price realization increased 57% to \$34.88 per barrel of equivalent oil (boe), and the netback increased 74% to \$32.31 per boe. The netback refers to the amount per barrel after production and transportation expenses. And revenue increased a whopping 65%.

Let's remind ourselves what the investment case is for Freehold Royalties.

First and foremost, the company represents a defensive way to gain energy exposure in our portfolios. The fact that the company's production is royalty focused (82% of production) means that this is a lower-risk business model, as the company does not pay any of the costs associated with this production.

Keep in mind that this royalty focus has just intensified; Freehold sold off 750 million boe per day of working interest production early in the second quarter.

What also makes Freehold a defensive name is its diversification. The company's royalty production is from over 30,000 wells and from over 200 operators. And the top payor represents less than 10% of total royalty revenue. Furthermore, the company still has a very strong balance sheet with a total debt-to-capitalization ratio of less than 10% and \$829 million in cash.

With regard to the dividend, the company instituted a 25% dividend increase early this year and is now paying \$0.05 per share in annual dividends. This represents a dividend yield of 4.28% and a payout ratio hovering in the 60% range, which is at the low end of the company's targeted 60-80%.

If we believe that the price of oil is headed higher or will even stay in this territory, then it would be reasonable to think that Freehold's dividend will be increased again. If, however, the price of oil drifts lower, the company still has room to maneuver to keep its dividend where it is. The point is that the downside in Freehold is not as extreme as other oil and gas companies' downside due to its business model.

Freehold is a defensive way to play the energy space. I think we can all agree that timing and predicting where the oil prices will go remains a very difficult thing to do successfully. There are many factors influencing oil, and so our best bet is to gain exposure in a way that limits the downside and focus on preservation of capital.

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1. Dividend Stocks
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