



Freehold Royalties Ltd.: Can Investors Expect an Increase in its 4.25% Dividend Yield?

Description

Freehold Royalties Ltd. ([TSX:FRU](#)) is a smart, defensive way to play the energy space. With a dividend yield of 4.25%, and diversified royalty production, the company has good upside to rising oil and gas prices with less downside than other energy names.

Freehold is a Canadian energy company that is engaged in the development and production of oil and gas, predominantly in western Canada. The company focuses mainly on acquiring and managing oil and gas royalties, and royalty interests currently account for 90% of total production and contribute 97% of operating income.

The company reported second-quarter results August 9, and benefited from a 16% increase in average price realizations to \$32.98 per barrel of oil equivalent (boe) and a 16% increase in royalty production to 11,270 boe per day.

This, coupled with the fact that cash costs declined 23% to \$5.63 per boe in the second quarter, meant that Freehold achieved a significant improvement in cash flow. Funds from operations increased 32% to \$31.8 million, and free cash flow increased to \$12.9 million.

And, as a reminder, because the company is focused on royalty production, it does not pay any of the costs associated with this production. Which makes it a lower-risk business model, leaving the company with this cash to pay dividends to shareholders and to pay down debt.

In fact, the company instituted a 25% dividend increase early this year (in March) and is now paying \$0.60 per share in annual dividends for a dividend yield of 4.25%.

Furthermore, the company was able to bring down its net debt, which now stands at \$50 million compared to \$98 million at the end of the second quarter of 2016. The company is also in the position to make additional acquisitions.

Looking to the future, the company has increased its production range guidance and reduced its operating cost guidance to reflect higher than expected production volumes.

So, what does this mean for investors?

Well, first of all, the company's dividend-payout ratio is currently 61%, which is at the low end of the company's targeted range of 60-80%. This puts the company in the position to consider instituting another dividend increase and/or to make another acquisition, which would likely lead to a dividend increase further down the line.

Freehold has a history of being an opportunistic acquirer, making over \$400 million in acquisitions in 2015 from Anderson Energy and **Penn West Petroleum Ltd.**, and the 2016 royalty acquisition from **Husky Energy Inc.**

With the company being in such a strong financial as well as operational position, I think investors can reasonably expect to see further increases in the dividend.

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