



Which Is the Better Buy: Baytex Energy Corp. or Freehold Royalties Ltd.?

Description

At the time of writing, crude oil is trading at just above US\$51, after the commodity broke the all-important \$50 mark and is maintaining its level, as reduced supply due to production cuts and increased demand expectations are taking hold.

The question of which stock is a better buy is sometimes very obvious, but other times, it depends on subjective needs and beliefs.

In this case, for example, we can see strengths with both of these names. **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) has an enviable asset base and operational momentum in its favour. **Freehold Royalties Ltd.** ([TSX:FRU](#)) has a strong, diversified portfolio of royalty payments from different producers and different areas.

Let's tackle Baytex first.

Baytex is actually achieving operational momentum, with production of 72,811 boe/d in the second quarter of 2017 — a 5% increase from the first quarter.

Oil at \$50 per barrel means Baytex is free cash flow neutral; at \$55 per barrel, it means incremental free cash flow of \$75 million; and oil at \$65 per barrel means incremental free cash flow of \$175 million.

The company has stated that if oil stays above \$50 for a sustained period, then the company would ramp up its drilling to take advantage of it.

The downside to Baytex is the fact that its balance sheet is heavily indebted with a debt-to-capitalization ratio of 48%.

Freehold is a smart, defensive way to play the energy space. With a dividend yield of 3.99% 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.

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 cash to pay dividends to shareholders and to pay down debt.

At the end of the day, the choice between these two names comes down to risk tolerance and your opinion on oil prices.

If you can accept an elevated level of risk, Baytex has the potential to provide exceptional returns. And the more conviction you have on oil prices strengthening further, the better Baytex looks.

Freehold is the more stable choice. It pays a nice dividend and has less downside, but that means less upside.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)
2. TSX:FRU (Freehold Royalties Ltd.)

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