Canadian Investors Have Become More Conservative. Case in Point: Baytex Energy Corp. (TSX:BTE) Stock

Description

With the share price of Canadian oil producer **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE) taking off in recent months, it has come as little surprise that the company would attempt to leverage its newly improved equity valuation to improve its market share position in Canada's oil and gas sector — a sector which has been hit very hard in recent years, making many companies appear like excellent long-term value plays at current prices.

Baytex's $1.4 billion acquisition of rival **Raging River Exploration Ltd.** has been touted by Baytex's management team as a "debt-improvement" play. The deal lowers Baytex's overall debt ratio due to the fact it will engage in an all-stock deal with Raging River, allowing the company to (in theory) seamlessly integrate the two firms and benefit from a combined debt structure, which will move from around three times annual cash flow to below two times. Baytex would thus be in range of the industry average 1.5 times cash flow with a few asset divestitures, or perhaps an equity issuance, should the firm attempt to leverage its share price further.

As it turns out, however, Canadian investors have proven to be less amused with this acquisition than may have been initially anticipated by Baytex's management team, resulting in a sell-off which saw the company lose approximately 17% since the acquisition was announced. While some of this decline may be due to the fact that investors don't believe now is the right time to increase exposure in this current environment, I think the majority of this decline is related to sentiment among many investors who have simply become more conservative overall.

While the global price of crude oil has steadied at a much higher level than what we have seen in the past 12-24 months, the reality remains that betting on the price of oil remaining above a certain level is a dangerous strategy. Investors in Baytex before 2014 can attest to this — companies with balance sheets that are significantly more levered than the industry average can be dangerous.

Bottom line

The recent rise in Baytex's stock price can be nearly entirely attributed to the improving commodity price environment for the oil and gas sector. This driver has proven to be unreliable in recent years, and investors appear to be hesitant to view all-stock deals as positive, especially deals that dilute their ownership in a company that was on track to reduce debt organically (and instead attempt to reduce debt ratios via acquisition).

At this point in time, I view Baytex's recent stock price rise as temporary and would encourage investors to look elsewhere for value, focusing on companies looking to reduce debt in an organic manner in this rising interest rate environment.

Stay Foolish, my friends.

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