Crude Bets: Baytex Energy Corp. (TSX:BTE) vs. Crescent Point Energy Corp. (TSX:CPG)

Description

Recently, crude has begun to undo the recovery that had taken place since oil's massive slide in 2014 and 2015.

For many who got burned during the previous decline, it was likely tough to stomach returning to energy names. That said, investors who renewed their bets on crude in early 2016, as WTI traded around US$30, have been rewarded handsomely.

Now, as oil tumbles, another opportunity has emerged to buy into energy at depressed prices. Those who missed out on crude's last rally are about to get a chance to ride the next one.

Once market darlings with shares trading above $40, Baytex Energy (TSX:BTE)(NYSE:BTE) and Crescent Point Energy (TSX:CPG)(NYSE:CPG) have been some of the hardest hit. Each now trade below $5. Still, investors remain hopeful that these companies might return to their former glory in an improved price environment.

The big question: Of the two, which is the better bet for an explosive turnaround?

Baytex Energy

The precipitous decline in Baytex shares during the previous oil slump was largely due to the poorly timed acquisition of Aurora Oil & Gas, for which the company paid a significant premium all while taking on about three-quarters of a billion dollars in Aurora's debt.

In June of this year, Baytex agreed to acquire Raging River Exploration in an all-stock deal that dealt another blow to its share price. While BTE shares were diluted by the deal, it improved the company's balance sheet and reduced its ratio of leverage to cash flow.

The primary reasons to believe in Baytex are its high-netback light oil assets. The company's operations in the Viking Formation and the Eagle Ford are immensely lucrative, and new wells in these areas quickly pay for themselves.

The doubters point toward Baytex's debt, its underperforming heavy oil assets, and its costly capital program. At roughly $2.1 billion as of September 30, the company's debt vastly exceeds its market capitalization. Add to the equation the drag of Peace River and Lloydminster heavy oil, together with capex that depends on WTI trading above its current price, and it becomes clear that skepticism is justified.

Still, it remains hard to ignore that Baytex is dirt cheap – trading at a price-to-book ratio of around 0.4 and only 0.5 times sales.

Crescent Point Energy

Presently, Crescent Point is undergoing a significant transition that aims to focus the company, cut costs, and reduce debt.

The company's roughly $4 billion in net debt is a going concern and CPG is aiming to get its ratio of debt to cash flow, which currently sits around two times, down to around 1.3 times over the course of the next couple years.

In order to achieve this goal, Crescent Point is looking to unload some of its weaker upstream assets. Further, the company is driving capital efficiencies – getting more barrels of oil out of each dollar spent in development.

Uncertainty surrounds management's ability to deliver on its stated target, just as it does the company's costly expansion projects in Flat Lake and Uinta Basin. Still, Crescent Point's core assets in Shauvanon and Viewfield Bakken generate healthy free cash flow with low costs.

Cut from $0.10 monthly to $0.03 in 2016, the company continues to pay a dividend that works out to a nearly 9% yield.

The verdict

Of the two stocks, I believe that Baytex is a better bet, but only by slim margin.

Geographical diversification is among the reasons that lead me to choose Baytex; the company is the only one with developed assets in the United States. Crescent Point's Canada-weighted portfolio exposes the company to risks such as getting their product to market, while their U.S. project in Utah is capital intensive and uncertain.

Also of note, I don't think that favouring Crescent Point due to its dividend is prudent. It seems likely to me that another protracted period of depressed oil prices would lead to a further cut or potentially an indefinite suspension of distributions.

Finally, I would like to note that an investment in either of these companies is speculative in nature. These stocks are not for those who cannot tolerate volatility. However, investors who have no trouble with risk may eventually see an immensely impressive turnaround.

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