Baytex Energy Corp. (TSX:BTE): Is the Stock Too Cheap to Ignore?

Description

Contrarian investors are constantly searching for beaten-up stocks with the potential to generate significant returns on a shift in fortunes or market sentiment.

The strategy comes with risks, as you don't want to get burned trying to catch a falling knife. However, the upside opportunity is attractive when an investor gets the timing right.

Let's take a look at **Baytex Energy** (TSX:BTE) (NYSE:BTE) to see if it deserves to be in your portfolio right now.

Oil rout

Oil prices have been on a rollercoaster ride over the past four years. In the summer of 2014, WTI crude traded for US$100 per barrel. A surge in shale production in the United States flooded the market and oil went into a steep decline, eventually bottoming out below US$30 per barrel in early 2016.

Oil producers saw their revenue and cash flow drop in step, and companies carrying significant debt took a big hit. Baytex is one of those names. The stock traded for $48 per share at the peak, and hit a low near $2 at the worst of the rout.

Since then, the share price has been volatile, making large moves up or down depending on oil market news or shifts in oil prices. Oil rallied from US$42 per barrel in the summer of 2017 to US$76 two months ago. A steep drop through October and November sent the price to a recent low of US$50. At the time of writing, WTI oil trades at US$53 per barrel. Baytex trades at $2.50 per share.

Where is oil headed?

The steep decline over such a short period of time appears overdone, and efforts to reduce supply could quickly send oil prices surging again. Heading into 2019 we could see oil begin to recover, and the new U.S. sanctions against Iran might shift the market balance.

Should you buy Baytex?

Baytex continues to carry significant debt, and that is not going to change quickly, unless oil prices in Canada and the U.S. can muster a strong recovery. Western Canadian Select (WCS) currently trades at US$17 per barrel, compared to US$53 for WTI.

On the positive side, management added strategic assets through the recent merger with Raging River Exploration and the team is doing a good job to improve the revenue situation. Baytex has agreements in place to move more of its Canadian production by rail through 2019. In the United States, Baytex has attractive assets in the Eagle Ford play in Texas. Production on these sites gets WTI pricing, so any improvement in WTI will have a positive impact on cash flow.

If you think oil is about to recover and have a bit of cash sitting on the sidelines for a contrarian pick, Baytex might be an interesting option at the current price. There is also a chance the company could become a buyout target, although I wouldn't buy the stock on the hopes of a big takeover premium.

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