Baytex (TSX:BTE) Is Cheap for a Reason, Making it an Energy Stock to Avoid

Description

Oil has performed strongly since the start of 2019 to see the North American benchmark West Texas Intermediate (WTI) up by 25% over that period and trading at US$56 per barrel. While that has been a boon for many energy stocks, including some Canadian drillers such as **Crescent Point**, others such as **Baytex** (TSX:BTE)(NYSE:BTE) are languishing at multi-year lows.

This has sparked speculation that Baytex is an attractively valued play on higher oil, making now the time to buy. While the $2.8 billion acquisition of Raging River Exploration in 2018 was beneficial for Baytex, the driller is cheap for a reason, making it an unattractive play on higher oil.

Weak balance sheet

A key issue facing the driller is its tremendous mountain of debt. Even after repaying around $200 million during the third quarter, Baytex's long-term debt totals around $1.7 billion, which is a worrying 2.4 times trailing 12-month adjusted funds flow.

Then there is the additional $980 million in other non-current liabilities, including leases, income tax, and asset retirement obligations. Baytex's non-current financial obligations total over $2.6 billion, which is a huge pile of debt for a company with a market cap of $879 million. This indicates that unless Baytex can significantly reduce debt, it is highly vulnerable to weaker oil and other economic ructions.

It should also be considered that Baytex is facing a series of near-term debt maturities, including US$400 million in 2021, an additional $300 million in 2022, and another US$400 million during 2024.

There is also its revolving credit facility with $413 million outstanding that is due to mature in April 2021. While there is every sign that lenders will renew that facility, it is not guaranteed after the difficult operating environment, poor outlook for oil, and growing likelihood of a global recession are considered.

Those maturities total around $1.8 billion, highlighting that Baytex may struggle to meet its financial obligations, unless oil recovers significantly in coming months.

According to the driller's 2019 guidance, Baytex needs WTI to average greater than US$50 per barrel over the course of the year to be free cash flow positive. While that is significantly lower than the US$57 a barrel averaged by WTI since the start of 2019, there are growing fears of another oil price collapse occurring in 2020.

If WTI fell below US$50 a barrel and remained there for a sustained period, it would derail Baytex's plans to accumulate sufficient free cash flow to meet its looming debt maturities. That would force the driller to make further asset dispositions at fire-sale prices in an unfavourable operating environment.

Another aspect of Baytex's operations that has ratcheted up the perceived degree of risk associated with investing in the driller is its significant exposure to Canadian heavy oil, which makes up 28% of its total hydrocarbon output.

During the second half of 2018, the Canadian heavy oil benchmark Western Canadian Select (WCS) plunged to record lows, as growing domestic oil supplies and lack of pipeline exit capacity caused a massive domestic supply glut to emerge.

The introduction of mandatory production cuts by Edmonton boosted WCS prices and reduced the surplus, but there are concerns that a similar event could occur once those cuts end. If WCS prices fall once again when the cuts end, which could be earlier than as planned, it would have a marked impact on Baytex's ability to generate free cash flow, impacting the driller's ability to meet its financial obligations.

Foolish takeaway

Baytex has made significant progress with shoring up its balance sheet and boosting more profitable light oil production. Its acreage in the Eagle Ford Basin, which is responsible for 43% of its production, is a very attractive asset, but Baytex will continue to struggle, weighed down by a burdensome debt load unless oil recovers soon.

The likelihood of WTI rallying to above US$60 per barrel during the immediate future is unforeseeable, and the rising threat of another oil price collapse is weighing on Bayex's outlook.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)

PARTNER-FEEDS

1. Business Insider
2. Msn
3. Newscred
4. Sharewise

5. Yahoo CA

Category

1. Energy Stocks
2. Investing

Date
2025/09/19
Date Created
2019/10/24
Author
mattdsmith