Baytex Energy (TSX:BTE): Could the Stock Price Finally Soar in 2020?

Description

The Canadian energy sector continues to struggle amid low oil prices and ongoing battles to get more pipelines built to deliver product to the United States and international markets.

The fallout, which began more than five years ago, has hammered the share prices of many of Canada's high-profile oil and gas producers. Stocks that once paid reliable and attractive dividends, now offer no payouts at all and trade at a mere fraction of their previous values.

Debt is the largest challenge for the group, as companies borrowed big bucks to make acquisitions that turned out to be very expensive bets. One name that stands out is **Baytex Energy** (TSX:BTE)(NYSE:BTE).

The company spent $2.8 billion in 2014 to buy Aurora Oil and Gas. The deal gave Baytex a strong foothold in the Eagle Ford shale play in Texas and was supposed to be a game changer for the company and its investors. In fact, the board raised the dividend by 9% when the acquisition closed in June of that year. At that point, the new annualized payout was $2.88 per share.

Unfortunately, oil began to fall from its US$100 per barrel price shortly after Baytex closed the Aurora Oil and Gas purchase and the boost in cash flow Baytex anticipated from the assets quickly evaporated.

High debt and falling margins created a cash flow crisis, and Baytex was forced to slash the distribution. By mid-December, the stock had fallen to $15 from the summer high of $48, and management scrambled to negotiate new terms with lenders.

A brief spike in oil prices in 2015 enabled Baytex to raise capital through an equity issue, and that might have saved the company. Since then, the share price has gradually continued its decline, with intermittent spikes on positive market sentiment followed by new lower lows.

At the time of writing, Baytex is down to $1.45 per share.

Opportunity?

When Baytex announced its 2018 year-end results in March, the company said its net asset value at December 31 was estimated to be $7.27 per share. If the company's calculations are correct, the stock could have some large upside potential on a takeover bid.

Baytex has made progress in its efforts to shore up the balance sheet. The company reduced net debt by $294 million, or 13%, in the first three quarters of the year. An uptick in oil prices through 2020 would boost margins and enable Baytex to continue chipping away at the debt position.

Given the depressed level of the shares, a move to $3 wouldn't be a surprise on positive news in the oil market.

Risk

Further weakness in oil prices would put more pressure on Baytex. In addition, the strike at **Canadian National Railway** is putting oil-by-rail shipments at risk. Baytex has 40% of its Q4 2019 production contracted to ship by rail.

At the time of writing, CN is still negotiating with employees. It is unlikely the strike will last longer than a few days, but the threat is worth considering when evaluating Baytex and other Canadian oil producers today.

Should you buy?

The stock certainly appears cheap, but anyone who'd bought the shares at previous lows and held on to them is now under water. Downside risks remain, and it wouldn't take much negative news to push the share price toward $1.

If you are positive on oil for 2020, a small contrarian bet might produce some nice short-term rewards on the next bounce, but I wouldn't back up the truck.

The TSX Index is home to other cheap stocks that might be better bets right now.

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