



1 High-Leverage Energy Play With Tonnes of Upside Today

Description

Right now, energy stocks are hot. Indeed, a bull market in commodities has taken energy prices on a nice ride. For long-term investors who bought the dip in the energy sector last year, congratulations.

For the rest of us who didn't, there's still opportunity in this sector today. Cash flows of many companies are soaring. And those with the most unfavourable balance sheets are getting re-rated higher.

One such company I think could have potential [near- to medium-term upside](#) is **Baytex Energy** ([TSX:BTE](#))(NYSE:BTE). Here's why.

Analysts increasingly getting bullish on Baytex

Analysts have historically not shown favourable ratings to Baytex in the past. The reasons are obvious. Indeed, the company's limited production and relatively high levels of debt have burdened investors during downturns in the energy market. Accordingly, last year was not a good year for Baytex shareholders.

However, the company has made some significant improvements of late. These moves warrant another look by investors who may have taken this stock off their watch list.

This company has de-risked its balance sheet significantly of late. The company is focused on profitable investment opportunities such as its clearwater play. Additionally, Baytex has focused on continued debt repayment over time. If the company can get its books in order, more fundamentals-oriented investors may be enticed by this play.

As a higher-cost producer, Baytex also benefits greatly from the current oil price environment. With oil trading around US\$70 WTI, Baytex has the potential for a triple-digit NAV increase this year. Analysts believe such a move could result in a re-rating for this stock higher. That is, if everything continues along perfectly, as it has, of late.

Consolidation bullish?

The idea of debt-laden companies making acquisitions isn't something I'm generally fond of. But for those who believe the energy sector has tonnes of room to run, perhaps the timing of deals right now makes sense.

Baytex recently acquired **Raging River Exploration** at a price of US\$1.4 billion. This combination should provide roughly three times the cash flow Baytex is used to. This deal will also provide even more leverage to oil prices than what the company already provides.

Accordingly, Baytex's ROI calculation is an intriguing one. For oil bulls, this is a no-brainer at this level. For more conservative investors unsure of where commodity prices are headed, it's less so.

Bottom line

Conservative investors have rightly steered away from Baytex in recent years. Indeed, the company's balance sheet still needs a lot of work.

However, deep-value investors have sought out Baytex stock as a unique buying opportunity in this environment. I think both viewpoints are valid. For investors intrigued with Baytex, whether to buy depends greatly on where one sees the price of oil in one, two, or five years from now.

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chrismacdonald

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