Baytex Energy: Is the Stock a Good Buy Right Now?

Description

Baytex Energy (TSX:BTE)(NYSE:BTE) has had a rough ride over the past seven years. As oil prices stabilize, contrarian investors are wondering if the worst is finally over. Let's take a look at the current situation to see if Baytex stock is now undervalued and deserves to be on your buy list.

Stock crash

Baytex traded for $48 in the summer of 2014 and paid out an annualized dividend of $2.88 per share. By the time it bottomed out in 2020, the stock hit a closing low near $0.30. That's a terrible performance, and investors who'd previously owned the stock for its attractive dividends still can't believe the carnage that occurred after oil prices crashed from their US$100-per-barrel peak.

The entire energy sector took a hit when oil tumbled in 2014, but Baytex really got hammered. Baytex closed a major acquisition in June that year, shortly before the price of oil started its plunge. The $2.8 billion purchase of Aurora Oil and Gas added strategic assets in the Eagle Ford shale play in Texas. At the time the deal closed, Baytex had high hopes for a boost to cash flow. The board even raised the dividend by 9% on the optimistic outlook.

Unfortunately, high debt levels and falling revenue forced management to eventually eliminate the payout. By the end of 2015, the stock was below $5. A few head fakes to the upside occurred in the years that have followed, but most investors who tried to call the bottom ended up getting burned.

To their credit, the Baytex management team moved quickly to mitigate the damage, and those efforts likely saved the company. For example, an equity issue at $17.35 per share in 2015 when oil briefly rebounded raised $600 million in capital, and lenders agreed to renegotiate terms.

Upside

A return to $40 per share is not likely, but investors who buy the stock near the current price of $2.20 per share might have a shot at some decent gains.

Baytex reported solid Q2 2021 results. The business generated $122 million in free cash flow in the quarter and reduced net debt by $129 million. Net debt at the end of the quarter was $1.63 billion. That's still pretty high, but the company can chip away at the debt position in a meaningful way as long as oil prices remain at current levels.

Management raised the 2021 production guidance for the year to as high as 80,000 barrels of oil equivalent per day (boe/d) while maintaining capital expenditures. Baytex now expects to generate $350 million in free cash flow this year.

Based on an average WTI price of US$55 per barrel Baytex expects to generate more than $1 billion in free cash flow through 2025. At US$60 per barrel, that amount jumps to $1.5 billion and to $2 billion at US$65 per barrel.

Net debt is expected to fall to a target of roughly $1 billion in 2023. Assuming oil prices hold or extend their gains, the outlook for the stock should be positive.

Should you buy Baytex stock now?

Volatility should be expected. The share price was as high as $2.58 in July and subsequently dipped below $2. That said, oil bulls might want to start nibbling on pullbacks.

Debt is coming down quickly, and the board could decide to restart dividend payments, as the balance sheet improves and the gusher of free cash flow continues. Baytex has a market capitalization of $1.25 billion at the time of writing. The company could generate that much in free cash flow in the next three years.

Based on that scenario, the stock looks cheap today.

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