



This Mid-Cap Might Be the Best Way to Play an Oil Recovery

Description

I don't know about you, but I like a good bargain. By that I mean I like to buy companies with good management teams at the helm, excellent growth prospects, and strong balance sheets to back it all up. With Canadian heavy oil trading at the largest discount to its U.S. counterpart in recent history, the beleaguered oil and gas sector presents a slew of bargain names with attractive risk/reward ratios. While some energy stocks are on [fire sale for good reason](#), one name that does not deserve to be trading where it's current at is **Torc Oil and Gas** (TSX:TOG).

TORC is a light-oil-based producer with operations mostly in the southern Saskatchewan region. This geographic detail is important, as this means TORC has access to the lighter crude oils from that area, which trade at better prices than Canadian heavy oil. For example, medium density oils like Saskatchewan's Midale are trading at US\$34 per barrel compared to sub-\$12 for Western Canadian Select. Moreover, TORC's product mix towards the lighter oils was also well reflected in its latest quarterly report, which showed a realized price per barrel of \$66.83, when combined with a 29% increase in production over last year, points to strong cash flow generation to weather this crude downturn.

As for its capital program, the company only drilled an additional three wells in the Cardium area in favour of the richer economics in southern Saskatchewan, which saw an additional 40 conventional wells drilled. Furthermore, although this quarter was a busy one for TORC, its total capital expenditures are still on track to achieve the guidance of \$185 million for 2018.

Finally, the higher realized prices and capital discipline has translated into cold, hard cash for TORC, which saw funds flow on a per-share basis increase 16% in the last quarter versus the year before (\$0.44 compared to \$0.39 per share). This cash flow profile bodes incredibly well for TORC's dividend prospects, [which are some of the best in the industry](#), with a payout ratio at a very manageable 67%. In fact, given what we've seen so far, I would not rule out a dividend increase in the near term, especially as oil begins to recover.

So, why the sell off? I believe the stock is trading where it is mostly due sector-wide bearish sentiment. While a rising tide tends to lift all ships, unfortunately the inverse is also true, as proven cash flow-

generating names with excellent well economics have fallen victim to the market malaise. On the bright side, TORC's valuation has not been this cheap in a long time. According to analysts, TORC is currently trading at roughly four times its debt adjusted cash flow — well below its long-term averages, and a bargain given the value of its future prospects.

With an enviable cash flow position and increased forward production guidance, TORC is definitely a name I would pick to weather the downturn and reward its investors through both capital gains and dividends.

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