2 Cheap Stocks for Big Dividends and Amazing Upside

### Description

The North American stock markets are hitting new heights while the energy sector — oil and gas stocks in particular — have fallen and staggered. Some mid-cap producers, including **Vermilion Energy** (TSX:VET)(NYSE:VET) and **Whitecap Resources** (TSX:WCP), now offer yields of 7-10% because of their low valuations. The companies have a production mix of about 43% and 15% natural gas, respectively.



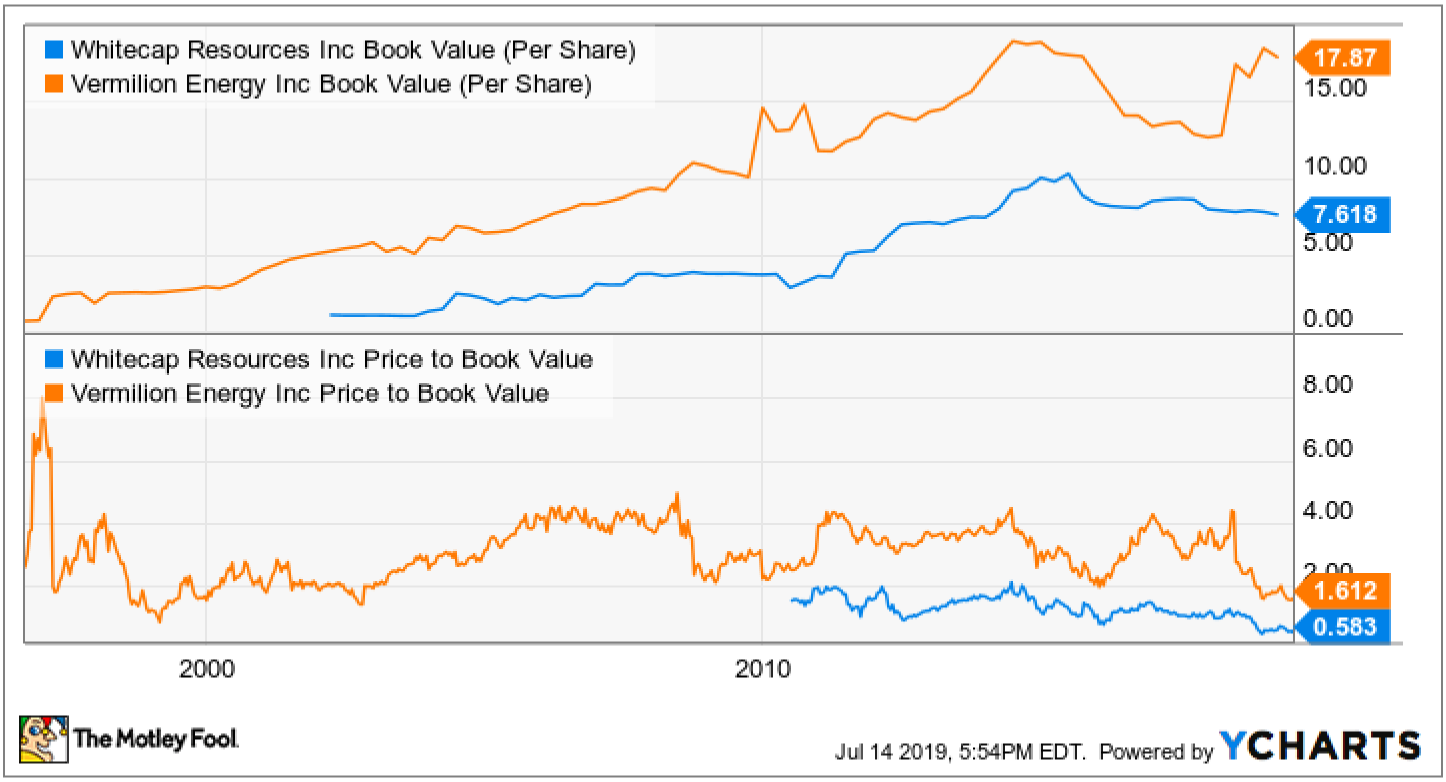
## Dirt-cheap valuations

The stocks have declined a lot in the last three months, but that by itself doesn't tell us whether the stocks are cheap or not.


*WCP data by YCharts.*



It's confirmed that the energy stocks are trading at historically low valuations from a price-to-book (P/B) perspective, while their book values have increased on a per-share basis in the long run.



*WCP Book Value (Per Share) data by YCharts.*

Assuming a more normalized fair multiple of three times book value for VET stock and 1.1 times for WCP stock, a fairer price for them would be $53.61 and $8.38, respectively. These targets imply upside potential of 88% for Vermilion and 89% for Whitecap.

Analysts have short-term 12-month targets of $41.50 and $8.32 per share, respectively, for the stocks, which imply near-term upside potential of 45% and 89%.

## Are their high yields sustainable?

Vermilion's dividend is reliable; since 2003, it has steadily increased its dividend per share by 35%. With the WTI oil price trading at US$55 per barrel or higher for most of the last 12 months, the company is expected to be able to generate enough cash flow to cover for its sustaining and growth capital spending and its dividends. It appears management puts a priority on sustaining capital before its dividends, while growth capital comes last.

Investors should note that Vermilion's timely acquisition of Spartan Energy in 2018 helped the company improve its cash flow generation on a per-share basis this year.



Thanks to some previous dividend cuts, Whitecap has a low payout ratio. In fact, it even increased its dividend per share by 5.6% in May. In the trailing 12 months, its free cash flow payout ratio was 46%.

## Foolish takeaway

The stocks of Vermilion and Whitecap stock are good choices to investigate further, because they can help patient investors make some serious money; they have relatively high (and safe) yields in the oil and gas space and incredible upside prospects.

Between the two, because of Vermilion's larger scale, it's been able to take on more leverage than Whitecap. If they both used all their operating cash flow to repay their debt, it would take Vermilion more than two years to do so while taking Whitecap less than two years.

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2. TSX:VET (Vermilion Energy Inc.)
3. TSX:WCP (Whitecap Resources Inc.)

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