



## Surge Energy (TSX:SGY) Could Deliver a More Than 132% Return in 2022

### Description

Canadian oil companies continue to benefit from surging commodity prices amid supply disruptions and rising demand. Most of the Top 100 stocks in 2022 belong in the red-hot energy sector. **Vermilion Energy**, **Baytex Energy**, and **Athabasca Oil** are among the high flyers.

However, **Surge Energy** ([TSX:SGY](#)) should be a buy target, as the small-cap stock could deliver more than its 132% year-to-date gain. On July 29, 2022, the energy sector advanced 2.9% to the lift the **TSX** to nearly 19,700. Surge Energy advanced 9.96% to close at \$10.16 per share.

Market analysts covering the \$847 million oil-focused exploration and development company have a 12-month average price target of \$14.54 (+43.11%). The surging energy stock also pays an attractive 4.55% dividend yield.

### Cash windfalls a strong possibility

According to Manav Gupta, a Credit Suisse analyst, the recent pullback of energy stocks was an attractive opportunity for investors. He thinks that only a global economic downturn can severely impact demand. If it doesn't happen, energy investors stand to benefit from the current constraints on global oil supply and elevated oil prices.

Gupta further added, "We continue to believe that in a post Russia-Ukraine conflict world, we are short of crude oil, refined products and natural gas. Energy companies will continue to rake in with cash windfalls from surging prices." Expect these conditions to support higher shareholder returns.

### Competitive advantages

Surge Energy takes pride in its high-quality light and medium crude oil reserves, production, and cash flow base. The low-risk, low-cost, low-decline conventional reservoirs are component advantages. According to management, combining them with disciplined capital-allocation strategies should result in significant free cash flow.

The company's ongoing concern is to develop high-quality, conventional oil reservoirs through a repeatable business strategy and a proven technology to enhance recovery through waterflood. Surge's exposure to Sparky and SE Saskatchewan, two of Canada's top five oil growth plays, provide exceptional economics and drilling inventory depth.

## Record financial results

The \$75.8 million cash flow from operating activities in Q2 2022 was a record for Surge Energy. It was an eye-popping 818% increase versus Q2 2021. Moreover, the adjusted funds flow of \$78.6 million represented a 479% year-over-year increase. Because of the \$36 million free cash flow (FCF), management was able to reduce net debt by 11.3% to \$280.1 million.

Management said the extremely tight physical market for crude oil is why there's continued growth in demand. It also noted that supply disruptions stem from years of global underinvestment in oil projects and ongoing geopolitical tensions. All these factors brought about a favourable commodity pricing environment.

Surge also paid its first monthly cash distribution (\$0.42 per share, per annum base dividend) during the quarter. The base dividend was 12% of the annualized cash flow from operating activities of over \$300 million in Q2 2022.

## Return of capital framework

Would-be investors can expect growing dividends from Surge Energy, as management implements the return-of-capital framework. The expiration of fixed price oil hedge volumes by year-end 2022 will provide incremental cash flow and FCF in 2023.

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#### **Date**

2025/09/18

#### **Date Created**

2022/08/03

#### **Author**

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