This Undervalued Energy Stock Offers a 9% Earnings Yield

Description

Segments of the Canadian energy market are deeply undervalued. Some stocks are cheap because investors have misunderstood the market dynamics. This could be an opportunity for a long-term investor to secure a bargain.

Here's an undervalued energy stock that should be on your radar.

Tourmaline

Calgary-based **Tourmaline Oil** (TSX:TOU) is an energy giant that's deeply undervalued. The stock has doubled year to date, but it still trades at just 11 times earnings per share. That implies an earning yield of 9%.

Much of the company's earnings are retained and reinvested. Tourmaline has used its excess free cash flow to pay down debt and improve its balance sheet. It has also used some cash flow to reward shareholders in the form of a special dividend of $6.7.

Excluding the special dividends, the stock's dividend yield is just 1.1%. This could be why investors have overlooked the stock.

Another potential reason for its undervaluation is that investors remain pessimistic about energy stocks. The recent pullback in oil prices may have dampened sentiments for the entire energy sector. However, Tourmaline's core natural gas operations are far more robust and deserve a better valuation.

Why natural gas?

There's a global shortage of energy. The production of both crude oil and natural gas lags behind demand. Russia's invasion of Ukraine and consequent sanctions have further entrenched this issue.

However, oil flows more freely across the globe. Russia has quickly diverted its oil exports to China and India over Europe. Natural gas, however, needs to be transported by pipeline infrastructure. Europe relies on the pipelines that have already been constructed to import energy from Russia. This isn't easy to replace because a pipeline with another country cannot be built overnight.

Turning the gas into a liquid is a potential solution. In fact, Canada and the U.S. have committed to building new liquified natural gas (LNG) facilities to transport energy to Europe. Qatar is doing the same. However, LNG is much more expensive than regular gas transported by pipelines.

Because of this, the value of natural gas has been far more resilient than crude oil this year. Natural gas is currently trading at $9.20 per million British thermal units. That's the highest level in 14 years. Meanwhile, crude oil is trading far below its $120 level. And demand for natural gas is likely to surge further in the months ahead as Europe enters winter.

These dynamics serve as tailwinds for Tourmaline. Last year, the company became Canada's largest natural gas producer. This year, the stock is still undervalued with more upside ahead. That's why Tourmaline stock deserves a spot on every value investor's watch list.

Bottom line

Natural gas prices are likely to be more resilient than crude oil, which is why Tourmaline is in a strong position for further gains. Keep an eye on this undervalued energy stock.

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