Will Vermilion Energy (TSX:VET) Stock Breach $50 This Year?

Description

Vermilion Energy (TSX:VET) stock is already topping the charts by a big margin. While TSX energy stocks have gained a massive 51%, beating broader markets this year, VET stock is sitting on 136% gains so far. And, interestingly, it seems well placed for even more growth this year and next.

VET stock is trading at a multi-year high

Vermilion is the only Canadian energy company that has significant exposure to Europe. Its higher production, mainly due to recent acquisitions and a strong price environment, will likely play well for its future earnings growth.

Note that despite the steep surge, some major growth drivers don't seem to have factored in the stock yet. So, Vermilion's discounted valuation seems quite profound and will likely create meaningful shareholder value, at least in the next few quarters.

Vermilion Energy reported strong free cash flows in the last few quarters. The cash largely went for debt repayments. The management expects its net debt to fall to $1.2 billion by the end of 2022 and to $850 million by 2023. As it reaches the leverage target, Vermilion will allocate a higher portion of its cash to shareholder returns. So, investors can expect higher dividend hikes and share buybacks.

Strengthening balance sheet and growing dividends

Driven by its strengthening balance sheet, Vermilion reinstated its dividend in the first quarter (Q1) and increased it further by 33% in Q3 2022. So, it will pay a total dividend of $0.32 per share this year, indicating a yield of 0.9%. That's way lower than its peers.

However, it is getting closer to where much steeper dividend growth will be delivered. And, importantly, investors would not mind slower dividend growth when the balance sheet is improving rapidly and the stock is trading at multi-year highs.

Deleveraging and dividend growth are common in the energy sector, so what makes Vermilion stand tall and outperform? Its exposure to Europe and recent acquisitions largely differentiate Vermilion from its peers. Vermilion announced an acquisition of 36.5% interest in the Corrib gas project in Ireland early this year. The transaction is expected to complete by Q4 2022. It is forecast to generate $361 million in free cash flows this year.

Apart from Corrib, Vermilion's Leucrotta acquisition is also expected to significantly benefit due to rallying energy prices. Leucrotta is an oil and gas exploration company with assets in British Columbia and northwest Alberta.

Interestingly, Vermilion has made these acquisitions without issuing equity or diluting existing shareholders. The timing of these acquisitions could not have been more fitting. The consolidated higher production and sky-high oil and gas prices should further accelerate Vermilion's free cash flow growth.

What's next for VET stock?

Vermilion's leverage levels are estimated to drop to pre-2008 levels by the end of this year. So, dividend growth will likely gain pace by Q4 2022 or by Q1 next year. Even if crude oil prices fall, its free cash flow growth offers visibility due to the strength in natural gas prices. Thus, balance sheet strengthening, solid expected earnings growth, and a supportive macro scenario will likely keep driving VET stock higher. And $50 levels, though they seem a tad steep, do seem possible.

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Date
2025/08/15
Date Created
2022/08/25
Author
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