2 Energy Stocks to Hedge Your TFSA in 2023

Description

Energy stocks have been on an incredible run over the past year, with many such names rallying in the face of the bear market. Indeed, energy has flexed its muscles after years of being outmuscled by almost everything else. With energy prices stabilizing in the US$80-90 range, many of the top producers could be in a spot to continue their outperformance relative to the TSX Index.

Indeed, the TSX Index has been given a nice jolt this year thanks to the run-up in energy stocks. Though chasing performance across various industries is never a good idea (nobody knows which industry will be top next year), I do think it's unwise to dismiss all the energy plays solely due to their past runs.

Undoubtedly, many TFSA investors are likely scarred from chasing momentum plays (think tech stocks) in the back half of 2021. By chasing the gains, one left themselves vulnerable to considerable downside. Indeed, some tech stocks shed well north of 80% of their value from peak to trough. Some innovation stocks lacking in fundamentals actually shed more than 90%.

It's dangerous to blindly chase momentum. However, in the case of energy stocks, valuations continue to be attractive. You see, many of the speculative tech stocks that folded this year didn't even have price-to-earnings (P/E) multiples to go by. Their valuations were a giant question mark. And without earnings, it was incredibly difficult to determine the right price to pay.

The case for buying energy stocks on strength

When it comes to energy stocks, P/E multiples remain depressed, with some top producers trading at single-digit P/E multiples.

P/E multiples may indicate "false value" if oil prices tank well below current levels going into the new year. Severe recessions tend to accompany weak demand for all sorts of energy. While energy could plunge as it did in 2014, I'd argue that for investors lacking any energy exposure that it's worthwhile to jump into the top producers at today's prices. If not for resilient, growing dividends, for the hedging benefits in an environment that continues to be inflationary.

Some smart minds (think Warren Buffett) are betting big on their favourite energy producers. While the value may not be as deep as their P/E multiples suggest, I still think they're more than able to improve a portfolio's risk/reward going into a recession year.

Consider **Canadian Natural Resources** (TSX:CNQ) and **Cenovus Energy** (TSX:CVE).

Canadian Natural Resources

Canadian Natural is an energy top dog that's just 7% from making new highs. The $89.8 billion energy kingpin trades at an absurd 7.9 times trailing P/E.

Despite soaring more than 55% over the past year, CNQ stock remains a terrific value assuming energy prices stay resilient going into 2023. Even if oil slips, CNQ has proven time and time again that it can manage through difficult times. The real question is how much ground the stock can run if the good times (higher energy prices) last for longer than the pundits expect.

With a 4.2% dividend yield and an improved growth runway, the stock is tough to pass up.

Cenovus Energy

Cenovus Energy has a smaller dividend yield (1.5%), but more upside in a scenario that sees oil prices stay elevated for longer. CVE is quite price-sensitive, but in today's environment, that's a good thing. The stock's down around 10% from its high just north of $30 per share. Though the dividend leaves a lot to be desired, it's subject to the greatest growth if it turns out oil's run has yet to enter its later innings.

Cenovus is a great TFSA hedge for investors willing to deal with excess volatility.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:CNQ (Canadian Natural Resources Limited)
2. TSX:CVE (Cenovus Energy Inc.)

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