



## This Small-Cap Energy Stock Has Risen 773% in 3 Years

### Description

The 2022 list of the 30 best-performing [growth stocks](#) featured 14 energy producers for the first time since 2019. However, one small-cap [energy stock](#) didn't join high flyers like **Obsidian Energy**, **Crew Energy**, and **Tourmaline Oil**, although it deserves the same attention.

**Headwater Exploration** ([TSX:HWX](#)) flies under the radar but has rewarded investors with far superior returns. At \$6.81 per share, the year-to-date gain is 32.23%, while the total return in 3.01 years is an eye-popping 773.1%. Had you invested \$15,000 three years ago, you would be \$115,961.54 richer today.

### Multi-year business strategy

Headwater is a developer and producer of petroleum and natural gas in Canada. The core operating areas are in Alberta (Clearwater, Marten Hills) and New Brunswick (McCully Field). The former boasts high-quality oil production, reserves, and lands, while the latter has low-decline natural gas production and reserves.

The \$1.56 billion resource company aims to deliver superior corporate-level returns by focusing on sustainability, asset quality, and balance sheet strength. Its multi-year business strategy is straightforward, and management wants to maintain positive working capital and add incremental prospects through accretive M&A (mergers and acquisitions) and strategic land acquisitions.

Headwater also hopes to provide a long-term return of capital stability with the continued implementation of secondary recovery, reducing decline rates. The last leg is to grow the quarterly dividend. After the solid financial and operating results for the three and nine months ended September 30, 2022, the board of directors has approved a return of capital strategy for 2023.

### Exceptional results

In the third quarter (Q3) of 2022, total sales and cash flow provided by operating activities increased

94% and 158% to \$94.95 million and \$72.06 million versus Q3 2021. Headwater's net income for the quarter rose 21% year over year to \$31.55 million. In the nine months ended September 30, 2022, the net income of \$122.32 million represents a 583% jump from the same period in 2021.

In Q3 2022, the average daily production increased 51% to 11,612 barrels of oil equivalent (boe/d). Also, at the quarter's end, Headwater's working capital was \$113.4 million, while outstanding bank debt was \$0. As mentioned earlier, the continued exceptional results prompted the implementation of the return of capital strategy.

## Inaugural quarterly dividend

Management is more confident now about the growth and return of capital, and it expects approximately 38% production per share growth in 2023 while underspending anticipated cash flow. Thus, the board declared Headwater's inaugural quarterly cash dividend (\$0.10 per common share) payable on January 16, 2023.

If the long-term West Texas Intermediate (WTI) oil price is US\$55 per barrel, Headwater is well-positioned to maintain its regular quarterly dividend. The forward annual dividend is 5.5%.

## Financial guidance

For 2023, the board-approved initial capital budget of \$200 million translates to an annual average production of 18,000 boe/d. Management expects to generate 38% production-per-share growth from a 60-70% reinvestment rate of next year's forecasted adjusted funds flow from operations (West Texas Intermediate oil between US\$75 and US\$85 per barrel).

Headwater forecasts adjusted funds flow from operations and free cash flow in 2023 to be \$285-\$330 million and \$85-\$130 million, respectively. Regarding the stock, the 12-month average price forecast of market analysts is \$9.89, or a potential 45.2% capital gain.

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1. Energy Stocks
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