Tourmaline Oil (TSX:TOU) Stock: How High Could it Go in 2023?

Description

Tourmaline Oil (TSX:TOU) was a top performer last year. The stock is up 62.7% over the past 12 months. Meanwhile, the **S&P/TSX Composite Index** is down 8.7% over the same period. Could this outperformance continue in 2023? If so, how high could the stock go this year? Here's a closer examination.

Key drivers

The energy crisis was a key driver of Tourmaline stock last year. Global demand for oil and natural gas was expected to rebound sharply as several economies reopened. However, Russia's invasion of Ukraine in early 2022 disrupted the global energy market and magnified the shortage. Natural gas prices have quadrupled since 2020.

As a result, Tourmaline experienced a windfall. Net profit and free cash flow were up 44% and 78% year over year respectively in the first nine months of 2022. The team shared some of this cash flow in the form of special dividends. In 2022, Tourmaline's total dividend payout was $7.65 per share, implying a 11.2% dividend yield based on its current market price.

However, natural gas prices have declined in recent months. Europe averted an energy crisis by securing stockpiles, while the winter was milder than expected. Each unit of natural gas is now trading at US$4.48 — less than half its was trading at just a few months prior. Unsurprisingly, this slump impacted Tourmaline's stock. It's down 18.9% since September 2022.

Looking ahead

The energy crisis may have been averted, but that doesn't mean the shortage has been resolved. Global energy supplies are still remarkably tight, which means prices could remain stable, if not rebound soon.

The International Energy Agency believes the European Union faces a natural gas shortfall of 30 billion cubic metres in 2023. To plug this gap, the continent will have to cut back usage or import liquified gas from Qatar and Canada. This effectively puts a floor on Tourmaline's revenue this year.

The company expects $3.7 billion in free cash flow in 2023. That implies a free cash flow yield of 16%. Meanwhile, management expects $12.13 in earnings per share (EPS) this year. That means the stock is trading at a forward price-to-earnings (P/E) ratio of 5.6. The three-year average P/E ratio for Canada's oil and gas sector is 16.4. Assuming Tourmaline achieves its EPS target, and the stock's P/E ratio rebounds to 10, each share could be worth $121.3.

Put simply, Tourmaline stock could double in 2023 based on conservative assumptions.

Bottom line

Tourmaline stock outperformed the market last year, but it's still undervalued. Tourmaline's fair value is significantly higher than current levels. It could double this year. Investors who expect a stable energy market in 2023 should add this underrated stock to their watch list.

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