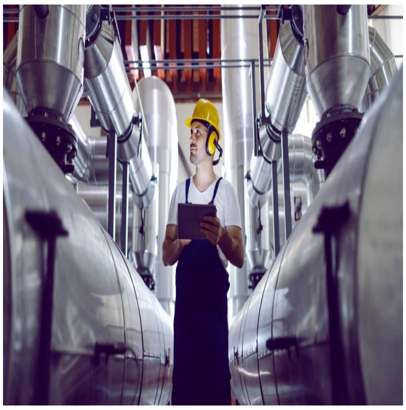

Parex Resources Stock: 1 Cheap Energy Stock That Pays a 5% Dividend

Description

Parex Resources (TSX:PXT) is a value stock that pays a nice dividend and could work well as a satellite holding in a diversified portfolio. It is an oil-weighted producer that's headquartered in Calgary, but its operations are in Colombia. Therefore, it benefits from premium Brent oil pricing. In fact, it is the largest independent operator in Colombia and has been in business for longer than a decade.

Market-beating returns potential but with higher risk

The energy stock is shareholder friendly. It has a track record of delivering shareholder returns. Its 10-year annualized returns are almost 14%, outperforming the Canadian market return by 5.8% in the period. But it did come with about 3.5 times the market volatility. Management anticipates to continue to return 100% of free funds flow to shareholders in the form of dividends and stock buybacks.

Notably, Parex stock just started paying a common stock dividend in the second half of 2021. The dividend should make its returns more reliable and its stock more stable.

Growth

In late 2021, it increased its land holdings by approximately four times. In so doing, it could drive higher long-term growth with the use of proven technology in exploration activities. Parex Resources is also expanding its portfolio through onshore gas opportunities.

For 2023, Parex Resources targets a production increase of about 15% to about 60,000 barrels of oil equivalent per day. Management also estimates an average well payout of only about eight months, including infrastructure spending. These short-cycle projects should provide protection from commodity price changes. The focus will be on minimizing decline and improving capital efficiency. Currently, it sees about 15 high-impact exploration prospects in its portfolio. Even without exploration upside, its existing portfolio could deliver base growth of 5% per year.

What's weighing Parex Resources stock?

One of the biggest drags on the oil stock includes the political risk in Colombia and windfall tax. This is why the stock is discounted versus the industry. Higher taxes would mean lower profits that result in less additions in retained earnings for the stockholders' equity.

The energy stock is down 17% in the last 12 months. At $19.90 per share at writing, it trades at about 3.6 times and 2.2 times, respectively, this year's estimated earnings and cash flow. The very cheap shares should lead to a successful stock-buyback program, which allows Parex to repurchase as much as 10% of its public float.

The Foolish investor takeaway

The company is poised to generate cash flows across various Brent oil prices. At US$60 per barrel, Parex can generate funds from operations per share of about $5 this year. At US$80 Brent, it can generate north of $6 per share. Currently, the Brent oil price just sit north of US$80 per barrel.

At the recent quotation, the consensus across 11 analysts believes the stock is discounted by over 40% and can potentially climb 74% over the next 12 months. Meanwhile, it also offers a nice yield of about 5%. For the trailing 12 months, its sustainable payout ratio was 21% of free cash flow.

In other words, for the higher volatility that shareholders endure, they could potentially pocket a 5% yield and strong price appreciation compared to something like a one-year Guaranteed Investment Certificate that pays a 5% interest income and guarantee of principal. Additionally, Parex Resources pay out eligible dividends that are favourably taxed in non-registered accounts versus interest income that are fully taxed at the marginal tax rate.

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