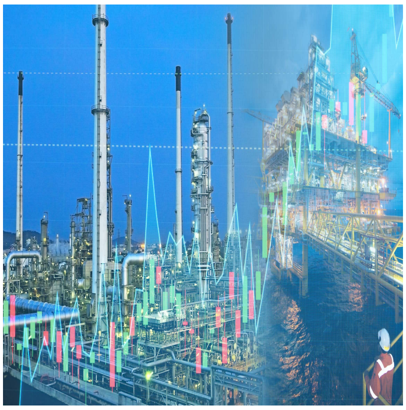

Energy Should Outpace Again in 2023: Here's a Top TSX Stock

Description

The corporate earnings growth outlook looks bleak for 2023 amid higher interest rates and recession fears. As a result, equities might continue to trade subdued this year after a weak 2022. However, at the same time, the oil and gas sector looks well-placed to deliver yet another stellar year. Their earnings growth, thanks to higher oil prices, will likely drive meaningful shareholder returns this year as well.

Will energy keep outperforming in 2023?

Crude oil prices tumbled in the second half of 2022, mainly due to excess supply from Russia and lower demand from China. The equation could reverse in 2023 with Chinese re-openings after months-long curbs.

According to the International Energy Agency's *Oil Market* Report in December 2022, the demand for oil will reach 101.6 million barrels per day, and supply will fall to 100.8 million barrels per day in 2023.

Rising rates and a recessionary environment notably weighed on global energy markets last year. This year, the picture on the macro front might relatively ease, and energy fundamentals should dominate.

Apart from higher oil prices, energy producer companies have become stronger since the pandemic. Just a few years back, oil and gas names were some of the disliked stocks as they burned significant shareholder wealth.

However, things have significantly changed. They have now become some of the most loved names across the street. And this is because rapid deleveraging and strong free cash flow growth have placed them on a more robust footing.

TSX energy stocks returned 50% last year, while markets at large tumbled 6%. Oil and gas could continue to outperform this year, driven by financial growth prospects and a strong price scenario.

Here’s a top TSX stock to bet on in the rallying energy sector.

#1 TSX energy stock for 2023

Canadian Natural Resources (TSX:CNQ) is one of my favourite TSX stocks in the energy space. It returned 45% last year, in line with Canadian energy bigwigs.

Thanks to its record free cash flow growth last year, CNQ increased its regular dividend twice and also issued a special dividend. It paid $4.9 billion in dividends and $5.7 billion in share repurchases. The energy producer has raised shareholder dividends for the last 23 consecutive years, a rare feat in a risky energy industry. CNQ stock currently yields 4.5%.

For 2023, CNQ aims to increase its production by 4% compared to 2022. Even if oil prices remain depressed, energy companies like CNQ will likely see superior earnings growth in 2023. This is because of their lower debt servicing costs and aggressive share buybacks. Note that CNQ’s net debt has been reduced by $8.9 billion since the beginning of 2021.

Valuation

CNQ stock is trading at seven times its earnings and a free cash flow yield of 10%. These valuation metrics imply a premium valuation compared to peers. However, it justifies the premium valuation driven by its scale and superior financials.

Despite its rich valuation, CNQ stock will likely keep topping charts due to its strong execution.

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