Is the Oil Boom Over?

Description

Crude oil has lost over a third of its value since June 2022. Unsurprisingly, Canadian oil and gas companies have also seen their market value diminish in these months. Is the energy boom over? Here's a closer look.

Energy outlook

The price of oil is driven by simple supply and demand factors. In recent months, there have been several surprises on both ends. Demand for energy was lower than expected as China's economy struggled and Europe experienced a mild winter. Meanwhile, the number of active drilling rigs in the U.S. quickly rebounded to pre-pandemic levels, and North America boosted exports of natural gas to Europe last year.

These factors could persist in 2023. If the world dips into recession, energy demand could be lower than expected. However, we still have supply constraints, which could keep the price of oil range bound for several years. That's a fair outcome for Canada's energy producers.

Small-cap energy stocks like **ARC Resources** (TSX:ARX) have already priced in all the concerns. That means they're either undervalued or fairly valued depending on your outlook. Regardless, these stocks offer lucrative dividends for income-seeking investors.

ARC's dividends

ARC Resources offers a 3.8% dividend yield at current prices. That's after the company boosted dividends by over 25% in 2022.

ARC's merger with Seven Generations Energy made it the largest condensate producer and the third-largest natural gas producer just in time for the energy boom. Now, the company is reaping the rewards. According to an analysis by **BMO Capital Markets**, ARC has a lower debt level and better credit rating than most of its peers in the energy sector. That should allow it to be more profitable and deliver better dividends for shareholders.

BMO also believes that companies like ARC can boost dividends this year. That’s because lower revenues from lower oil prices are offset by lower interest costs as these companies have paid off much of their debt. Put simply, ARC is still an excellent choice for income-seeking investors.

ARC stock valuation

ARC trades at a trailing price-to-earnings ratio of 4.8. However, that absurdly low figure is based on last year’s elevated oil prices. It could be fair to assume that earnings will dip mildly in the year ahead. That’s why the forward PE ratio could be higher.

According to calculations by Eric Nuttal, ARC Resources could generate a free cash flow yield over 15% – it currently trades at an enterprise value-to-free cash flow ratio of 2.8 –if the price of crude oil is over U.S.$80.

Put simply, ARC is a reasonably priced income stock. If the price of oil remains steady, this stock could deliver reasonable rewards for shareholders.

Bottom line

The energy boom is over, but the market is far from a bust. Demand may be lower; however, supply constraints remain. Canada’s small-cap energy stocks like ARC Resources may deliver steady (but not exceptional) returns in the year ahead.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:BMO (Bank of Montreal)
2. TSX:ARX (ARC Resources Ltd.)
3. TSX:BMO (Bank Of Montreal)

PARTNER-FEEDS

1. Business Insider
2. Flipboard
3. Koyfin
4. Msn
5. Newscred
6. Quote Media
7. Sharewise
8. Smart News
9. Yahoo CA

PP NOTIFY USER

1. cleona
2. vraisinghani

Category

1. Energy Stocks
2. Investing

Date
2025/08/12
Date Created
2023/01/27
Author
vraisinghani