Tourmaline Oil Stock: How High Could It Go in 2023?

Description

Some of the last year's top gainer energy stocks have been on a decline recently. Leading natural gas producer **Tourmaline Oil** (TSX:TOU) is one of them. TOU stock returned 80% last year but has dropped 26% since October 2022. And not only Tourmaline but almost all gas-focused energy producers saw a similar weakness of late. That's because warmer weather and excess supply weighed on gas prices, which have lost 75% since August 2022.

What's next for TOU stock?

Notably, Tourmaline is an appealing name even in a low-price environment. It may not see stunning value creation like last year. But the stock will likely remain relatively strong compared to peers and outperform.

Tourmaline is a $21 billion natural gas producer that aims to produce 530,000 barrels of oil equivalent per day in 2023. It also produces oil, natural gas liquids, and condensate and the production mix plays well for diversification.

Tourmaline Oil saw record financial growth last year thanks to higher energy prices. Its free cash flows came in at $2.7 billion in the last 12 months, representing an increase of 217% compared to 2021.

It plans to release Q4 2022 earnings on March 7. Apart from its stellar financial growth, investors can expect further strengthening of its balance sheet. Whether it can continue paying special dividends like last year remains to be seen. However, TOU offers handsome total return prospects in 2023 as well, driven by its handsome free cash flow growth potential.

What's special about Tourmaline Oil?

Tourmaline Oil stands tall among its peers mainly because of its high-quality assets. It has decades of low-cost drilling inventory, which is profitable even in a low-price environment.

Moreover, it sells its production in premium markets like California, which obtains a much higher rate than in the Canadian gas market. As a result, TOU stock has lost 25%, while natural gas prices have corrected by 75% recently.

For 2023, Tourmaline management expects free cash flows of $2.6 billion, lower than in 2022. However, a major chunk of this cash will be used for shareholder dividends as the net debt target has already been achieved. Free cash flow is the difference between cash flow from operations and capital expenditure. Free cash flows are used for dividends, mergers and acquisitions, and debt repayments.

Tourmaline has paid almost $1.5 billion in debt repayments since the pandemic, which has substantially improved its balance sheet. Its low leverage and earnings visibility make it a strong name in the Canadian energy space.

TOU stock also looks attractive from a valuation standpoint after its recent correction. It is currently trading at a free cash flow yield of 12% and looks discounted. On the price-to-earnings front, it is trading four times its 2023 earnings and indicates undervaluation. Even if some TSX energy stocks look cheaper than TOU, its financial growth prospects and dividends offer higher value creation potential.

Foolish takeaway

Even if natural gas prices remain weak, TOU stock might have a limited downside. Analysts have given it a price target of $92, indicating an upside potential of 50%. Its Q4 2022 earnings and management commentary will be essential to watch. How management sees its dividends shaping in 2023 amid low gas prices will be interesting to see. TOU stock is an appealing bet for the long term, given its high-quality assets, sound balance sheet, and free cash flow growth.

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vinitkularni20