EQUITY RESEARCH

Capital Markets

RBC Energy & Utilities Equity Team
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Global Energy Best Ideas

Our view: In March, the RBC Global Energy Best Ideas List was down 4.2% compared to the iShares S&P Global Energy Sector ETF (IXC) down 1.2% and a hybrid benchmark (75% IXC, 25% JXI – iShares Global Utilities ETF) that rose 0.4% on a sequential basis. Since its inception in February 2013, the RBC Global Energy Best Ideas List is up 124.0% compared to the S&P Global Energy Sector ETF up 23.4%.

Total Return Comparison	March	YTD	Inception
iShares S&P Global Energy (IXC)	-1.2%	-3.2%	23.4%
Hybrid Benchmark (75% IXC, 25% JXI)	0.4%	-2.3%	39.3%
RBC Global Energy Best Ideas	-4.2%	-5.7%	124.0%

March List Changes:
Additions: N/A
Removals: HTG-LN

RBC GLOBAL ENERGY BEST IDEAS LIST

	Ticker	Rating[1]	Analyst	Mkt Cap (mn)	Date Added	Add Price	Current Price	Price Target
Integrated Energy								
Repsol	REP-ES	OP	Borkhataria	€18,829	12/7/22	€14.52	€14.19	€20.00
Shell	SHEL-LON	OP	Borkhataria	£158,348	7/1/20	1,224p	2,309p	2,900p
Suncor Energy	SU-CA	OP	Pardy	C$55,677	3/1/23	C$45.86	C$41.96	C$55.00
Exploration & Production								
Tamarack Valley Energy	TVE-CA	OP	Davis	C$2,198	7/6/21	C$2.57	C$3.95	C$7.00
Topaz Energy	TPZ-CA	OP	Davis	C$2,754	11/1/22	C$23.04	C$19.11	C$28.00
California Resources Corporation	CRC-US	OP	Hanold	$2,737	6/1/21	$29.01	$38.50	$65.00
Diamondback Energy	FANG-US	OP	Hanold	$24,816	12/7/22	$138.21	$135.17	$182.00
Permian Resources Corporation	PR-US	OP	Hanold	$5,869	12/7/22	$8.99	$10.50	$14.00
Range Resources	RRC-US	OP	Hanold	$6,369	7/6/21	$16.76	$26.47	$40.00
ARC Resources	ARX-CA	OP	Harvey	C$9,496	5/1/21	C$7.73	C$15.33	C$26.00
Tourmaline Oil	TOU-CA	OP	Harvey	C$19,037	1/1/20	C$15.08	C$56.32	C$89.00
Canadian Natural Resources	CNQ-CA	OP	Pardy	C$82,466	4/1/22	C$77.41	C$74.79	C$89.00
Enerplus Corporation	ERF-US	OP	Pardy	$3,116	6/1/22	$14.84	$14.41	$21.00
Santos Limited	STO-AU	OP	Ramsay	A$22,780	6/1/19	A$6.74	A$6.90	A$10.00
Oilfield Services								
Liberty Energy	LBRT-US	OP	Mackey	$2,256	8/3/22	$14.20	$12.81	$26.00
SLB	SLB-US	OP	Mackey	$69,731	1/4/22	$29.95	$49.10	$66.00
Midstream								
Pembina Pipeline Corporation	PPL-CA	OP	Kwan	C$24,094	9/1/22	C$46.38	C$43.78	C$58.00
Targa Resources Corp.	TRGP-US	OP	Schultz	$16,533	12/1/21	$51.63	$72.95	$110.00
Cheniere Energy Inc	LNG-US	OP	Scotto	$38,408	5/1/20	$46.69	$157.60	$205.00
Energy Transfer LP	ET-US	OP	Scotto	$38,590	2/1/22	$9.57	$12.47	$17.00
Utilities, Refiners, Infrastructure & Renewables								
Superior Plus	SPB-CA	OP	Ng	$2,247	12/7/22	$9.82	$11.14	$15.00
Marathon Petroleum Corporation	MPC-US	OP	Schultz	$60,073	12/7/22	$109.29	$134.83	$146.00
PG&E Corporation	PCG-US	OP	Tucker	$32,142	9/1/22	$12.33	$16.17	$20.00
Drax Group plc	DRX-LON	OP	Wheeler	£2,437	5/1/21	409p	608p	1,030p

1-OP = Outperform, 2-Indicates Speculative Risk. 3-Opening price given is the closing price of the trading day prior to which the stock was added. 4-Return assumes all dividends and distributions are reinvested.
Note 1: Performance returns do not take into account relevant costs, including commissions and interest charges or other applicable expenses that may be associated with transactions in this Equity Best Ideas list. Past performance is not, and should not be viewed as, an indicator of future performance.
Source: RBC Capital Markets estimates, FactSet

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This Month’s Removals from Energy Best Ideas List

Exhibit 1 - This Month’s Removals

Hunting Plc (HTG) Victoria McCulloch, Analyst +44 207 429 8530 victoria.mcculloch@rbccm.com	• HTG-LN has been removed following a decrease in share price of >20% since it was added to the list according to our mandatory stop loss mechanism.

Investment Highlights

Below, we provide a summary of our analysts' views on each *Best Idea*.

ARC Resources (ARX)
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- **FCF generation ample.** ARC is set to generate ~$1.6 bn FCF in 2023 on our numbers. With a strong balance sheet and large M&A on hold (for now), the focus remains on Attachie development and RoC initiatives. ARC targets return of capital in the range of 50–100% of FCF via base dividend tied to earnings growth (now at $0.60/share), and share buyback. Production growth is not a specific target but rather an outcome of the most efficient way to execute projects (Sunrise, Attachie), paired with the Basin's capacity to absorb new product, and is unlikely to exceed 5%. See our recent quarterly note here.
- **Western Canada's largest Montney player.** ARC's production base of approximately 350,000 boe/d makes it what we view as a Montney Champion with top-decile supply costs and deep project inventory. This benchmarks ARC as the largest Montney producer, the third-largest outright gas producer, and the sixth-largest E&P by volume amid the WCSB producer landscape, with operated facilities network of ~1.5bcf/d—second only to CNQ and TOU. See our notes here and here.
- **Facility portfolio adds scale and optionality.** Following the absorption of 7G assets, ARC's owned and operated facility portfolio roughly doubles to about 1.5 bcf/d—now third in the basin behind CNQ and TOU. This larger strategic footprint allows for continued top-quartile operating metrics and optimized marketing, and it establishes critical mass, opening the door for other potential strategic options in the future. See our note here.
- **LNG – The key to long-term value creation.** ARC's existing 2P reserve book contains sufficient resource to sustain an entire 2-train LNG project (1.8 bcf/d) for 10+ years, and when adding future drilling could increase to 40–50 years. Accordingly, the company should be viewed as a key supplier, or alternatively as a strategic asset for operators looking for vertical integration. The owners of LNG Canada now collectively hold enough product to support Phase 1 of the development (~1.8 bcf/d), but any expansion (Phase 2, +1.8 bcf/d) would need to be augmented. ARX signed a Memorandum of Understanding with the proposed Cedar LNG Project for a 20-year LNG supply agreement to send 200 mmcf/d of natural gas, which is expected start in 2028/2029. See our notes here and here.

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Canadian Natural Resources (CNQ) Greg Pardy, Head of Global Energy Research (416) 842-7848 greg.pardy@rbccm.com	• **Globally distinguished.** Canadian Natural Resources' management committee structure and shareholder alignment are unique factors that distinguish the company globally. CNQ's long-life, low-decline portfolio—anchored by low sustaining capital—affords the company superior free cash flow generation throughout the cycle. • **Impressive shareholder returns.** CNQ is currently allocating 50% of free cash flow (after dividends and base capital) to share repurchases, with the balance (less strategic growth capital/acquisitions) earmarked for debt reduction. Once CNQ's net debt falls to $8 billion, the company plans to allocate 80–100% of its free cash flow as incremental returns to shareholders. Additionally, alongside fourth-quarter results, CNQ raised its common share dividend by 6% to an annualized rate of $3.60 per share. We think it is important to point out that CNQ has never cut its common dividend, which has grown at a CAGR of approximately 21% over the last 23 years. • **Strong alignment.** CNQ has no CEO. Instead, the company is stewarded by a management committee. This group meets weekly and oversees all matters encompassing marketing, finance, ESG, operations, and technology, among others. • **ESG – lots of progress.** CNQ has established a GHG emissions reduction target of 40% of total corporate absolute Scope 1 and 2 GHG emissions by 2035 (vs. a 2020 baseline). Not to be overlooked, CNQ also continues to make progress toward its initiatives with respect to the Oil Sands Pathways to Net Zero Alliance. CNQ also continues to target a 50% reduction in North American E&P (including thermal in-situ) methane emissions by 2030 (vs. 2016), and a 40% reduction in both thermal in-situ fresh water usage intensity and mining fresh river water usage intensity by 2026 (from a 2017 baseline).
Cheniere Energy, Inc. (LNG) Elvira Scotto, Analyst (212) 905-5957 elvira.scotto@rbccm.com	• **Highly contracted cash flow with strong counterparties.** Cheniere has a weighted average contract duration of 17 years on its long-term take-or-pay contracts and is 90% contracted on its nine-train portfolio including medium-term and short-term SPA and IPM agreements. All of Cheniere's Sale and Purchase Agreement customers are investment-grade rated or have investment-grade credit metrics. Importantly, utilities or state-owned utilities/oil and gas companies represent 68% of Cheniere's contracted capacity. • **Liquefaction fees represent most of Cheniere's EBITDA.** Cheniere's customers have the contractual right to cancel cargoes but still must pay fixed liquefaction fees. In our 2024 run-rate scenario, on a consolidated basis, liquefaction fees represent ~90% of Cheniere's total EBITDA while lift represents ~5% and marketing ~5%. • **Long-term FCF and capital return story with a growth option.** We believe long-term take-or-pay contracts with high credit quality counterparties provide cash flow visibility. After completing its 2021 capital allocation strategy ahead of schedule, Cheniere updated its capital allocation strategy, which now includes: (1) continued debt pay-down to hit a long-term run rate leverage target of ~4.0x Debt/EBITDA; (2) an incremental $4BN of share repurchase over three years; and (3) annual dividend growth of ~10% through the mid-2020s and target ~20% payout ratio once Corpus Christi Stage 3 hits run-rate cash flow. In addition, Cheniere continues to pursue potential growth opportunities with Corpus Christi Midscale Trains 8 and 9 as well as the Sabine Pass Liquefaction Expansion project in FERC pre-filing.

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Drax Group plc (DRX)

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- **Financials remain above consensus post EGL; biomass cost adjustment a big plus.** Clarity on the Electricity Generator Levy (EGL) provides greater visibility for Drax going forward, whilst the government's decision to allow for the changing cost of biomass within the EGL further removes uncertainty from the investment case. We think overall the EGL was significantly less draconian than the market anticipated and the allowance for changing biomass costs above a £65/MWh threshold is a key positive. We continue to take a conservative view on power prices, assuming a 20% discount to the forward curve, and therefore see further upside on a mark-to-market basis.
- **Three-pronged growth strategy continues to take shape.** Drax retains a number of growth options going forward, which include BECCS, new pumped storage capacity at Cruachan, and continued expansion of upstream pellet facilities. The development of BECCS continues to progress both domestically and internationally. In the UK, successful track 1 BECCS projects will be shortlisted in Q1-23 and we should also gain further clarity on the government's investment framework, which is likely to include a CfD mechanism for both power generation and negative emissions. Internationally, the regulatory framework in the US appears to be increasingly favourable for expansion of BECCS going forward. Additionally, new pumped storage capacity through the 600MW expansion of the Cruachan II pumped storage facility should be completed by the end of the decade. We see the £3bn capex growth plans as fully funded under the current balance sheet, with FCF yields averaging ~25% across the remainder of the decade.
- **Sustainability paramount to Drax's strategy.** Biomass continues to be a key part of the UK government strategy to achieve net zero, whilst Drax is leading the way on BECCS, which has growth potential both in the UK and internationally. We think criticism of Drax's sustainability credentials were inaccurate in the BBC Panorama documentary toward the end of last year, and we were reassured by a recent trip to see Drax's pellet operations first hand. Drax retains an active aim of ensuring that any biomass sourced will have positive outcomes for climate, nature, and the communities in which it operates.

Energy Transfer (ET)

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- **Energy Transfer is a publicly traded partnership that owns and operates a portfolio of assets across the natural gas, natural gas liquids, and crude oil value chain.** We believe ET is well positioned to generate meaningful cash flow growth as large-scale growth projects come online and as we expect growth capex to slow. With a stronger balance sheet, ET should be in position to return more cash to unitholders via distribution increases and/or unit repurchase.
- **Significant synergy potential from recent Enable Midstream acquisition.** (1) Enable brings additional demand pull transportation and storage assets in the Mid-Con and ArkLaTex regions. (2) Enable's Gathering and Processing assets in the Mid-Con complement ET's Gulf Coast fractionation and export assets. (3) Enable's Haynesville Gathering and Processing assets and its Gulf Run pipeline increase exposure to the global liquefied natural gas markets. (4) In the Bakken, Enable provides crude gathering that connects into DAPL. ET expects the Enable acquisition to generate $100MM of cost and efficiency synergies, which we view as achievable given the complementary asset bases.
- **Strong balance sheet FCF generation potential positions the company for capital return.** ET lowered its outstanding debt by ~$6BN in 2021 and exited 2021 with leverage of 3.9x (credit facility calculation) while targeting leverage of 4.0–4.5x. We forecast ET exits 2022/2023 with Net Debt/TTM Adjusted EBITDA of 3.7x/3.6x while paying $6.6BN in distributions.

Enerplus Corporation (ERF) Greg Pardy, Head of Global Energy Research (416) 842-7848 greg.pardy@rbccm.com	• **Solid all-around.** Enerplus remains our favourite intermediate producer given its capable leadership team, solid execution, strong balance sheet, and rising shareholder returns. • **FCF and shareholder returns.** Enerplus has always maintained a strong balance sheet and is now bolstering its shareholder returns offering. Commensurate with fourth-quarter results, the company reaffirmed its commitment to distribute at least 60% of free cash flow in 2023, with an accent on share buybacks. The company's net debt (debt less cash) stood at $221.5 million as of December 31. Execution of a substantial issuer bid (SIB) also remains an option for Enerplus as market conditions dictate. We peg Enerplus's free cash flow (before dividends and including A&D) at approximately $737 million in 2023. • **Bakken positioning.** Enerplus recently framed 655 drilling in its core/extended core areas of the Bakken—or greater than a decade of drilling inventory at the development pace factored into its five-year plan. • For our most recent update on Enerplus, please see "Finishing Strong".
Liberty Energy (LBRT) Keith Mackey, Analyst (403) 299-6958 keith.mackey@rbccm.com	• **Improving operational execution.** Completion of integration efforts with regard to the company's 2021 acquisitions alongside improved operational execution has enabled the company to materially outperform Street expectations in 2022. We expect strong results to continue into 2023 given strong demand for the company's pumping, sand, and logistics businesses. • **Tight frac market drives strong profitability.** Liberty has been able to capitalize on a tight pressure pumping market and expects to generate 40–50% y/y adj. EBITDA growth in 2023. We estimate the US horsepower market to remain relatively tight at approximately 14.5MM demand vs. 15.8MM supply in 2023. • **Compelling valuation.** Liberty is trading at a discount to its historical range and our frac services coverage peer set. In our view, Liberty should trade at a premium to frac peers given its larger scale, increasing vertical integration, strong balance sheet, and broad exposure to key North American basins. • See our latest Liberty Energy note here.
Marathon Petroleum Corp. (MPC) TJ Schultz, Analyst (512) 708-6385 tj.schultz@rbccm.com	• **Capital returns.** MPC has remained focused on returning capital to shareholders in the form of dividend payments and share repurchases. MPC increased its quarterly dividend by 29% to $0.75/share (from $0.58/share) in 3Q22, which is ~$370mm/quarter. MPC has repurchased a significant number of shares, which has resulted in multiple incremental increases of its share repurchase authorization, and has ~$7.6B remaining as of 1/31/23. We continue to expect MPC to be active on the incremental buyback authorization near term, with a clear preference for buybacks as a means to return capital. • **Renewable fuels.** MPC has continued to progress on the Martinez renewable fuels conversion project, expecting the first phase to reach full capacity of 260mm gal/yr by the end of 1Q23 and capacity to reach 730mm gal/yr by the end of 2023. MPC is well into its pre-fill strategy, pre-filling since mid-summer 2022. • **Constructive refining margins.** Along with the rest of the refiner group, MPC has benefited from improved refining margins from higher cracks and wider spreads. We expect these positive margins to continue into 2023 above historical mid-cycle levels.

Pembina Pipeline Corporation (PPL) Robert Kwan, Analyst (604) 257-7611 robert.kwan@rbccm.com	• **Positioned to benefit from higher WCSB production.** Whether it be uncontracted capacity or within its contract structures that blend minimum take-or-pay levels with fee- for-service upside as volumes grow, we expect Pembina to benefit from growing gas and liquids volumes in the Western Canada Sedimentary Basin (WCSB). Further, growing volumes could result in contracted infrastructure opportunities including NGL fractionation expansion and/or pipeline expansion projects. • **Free cash flow generation after all capex and dividend payments provides a range of capital allocation opportunities.** In 2022, the company prioritized share buybacks with the strategy going forward focused on creating balance sheet optionality by reducing leverage. Lower debt levels should position the company to pursue a wide range of growth initiatives on an equity self-funded basis. • **Solid base of business with a commodity kicker.** Pembina's guardrails target more than 80% of EBITDA coming from fee- based revenues, primarily underpinned by take-or-pay or cost-of-service contracts, which underpin the dividend. As upside optionality, Pembina's Marketing division can benefit from leveraging its asset base to take advantage of various commodity spreads.
PG&E Corporation (PCG) Shelby G. Tucker, Analyst (212) 428-6462 shelby.tucker@rbccm.com	• **Continued reduction of wildfire risk.** The company continues to execute on its wildfire-mitigation plan. Mitigation actions include system hardening, undergrounding, vegetation management, enhanced powerline safety settings, and public safety power shutoffs. • **Steep discount not warranted given that CA wildfire protections limit financial risk**. We believe the Wildfire Fund provides meaningful protections against financial liabilities associated with wildfires. While the market appears to remain apprehensive around the mechanics of the fund, we believe the multi-turn discount is overly punitive when considering the financial risks associated with a catastrophic fire. • **PG&E slowly rebuilding trust.** While the name remains overly sensitive to headlines, we have also seen a meaningful shift in tone from media and stakeholders. We believe this is a result of PG&E's continued efforts to engage stakeholders and communities and we are encouraged by positive signals from the CA legislature and regulator. • **Robust capex plan drives earnings growth.** PG&E expects above-average rate base growth at a 9% CAGR. Growth opportunities come from system hardening, undergrounding, electrification opportunities, and other wildfire-mitigation investments. Management targets 2% O&M reductions, which should act to help offset customer bill increases.

Repsol SA (REP)
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- **Refining exposure.** The advantages of Repsol's complex refining system were evident in 4Q, capping off a strong year with a refining margin premium higher than at any point in the last ten years. In the near term, our model for Repsol's refining margin suggests Q1 margins in the region of $16.50/bbl, with our calculations suggesting that margins have drifted higher in recent weeks. This is likely to be supportive for near-term earnings.
- **Commitment to shareholder returns.** Repsol's CEO struck a bullish tone on the 3Q call with intentions to reduce share count closer to 1,200m shares (vs. 1,452m at the end of 3Q22). This firm commitment suggests to us the possibility of material share buybacks as we look into 2023–24, which we expect to be well supported by strong organic free cash flow generation. As such, our forecast buybacks for Repsol of €2bn in 2023 map to total shareholder returns toward the top end of the pack, and we see the buyback activity providing an additional layer of support to the stock throughout the year.
- **Recent track record on inorganic activity.** Our sum-of-the-parts valuation for Repsol, which includes some punitive discount rates on the upstream division, is closer to €22/sh. Along with this, the company's recent partial divestments of its low-carbon portfolio and upstream divisions provide markers that suggest an undervalued share price and scope for a run-up from here.

Santos Limited (STO)
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- **Merger with Oil Search last year has created a top 20 global energy company** with 2P reserves of ~1.4 billion boe and 2022 sales volume of 112 mmboe. The transaction has delivered a more diversified production base (47% LNG, 35% gas, and 18% liquids) and improved growth profile (Pikka Alaska oil, Papua LNG, Dorado oil and gas). Santos's larger combined balance sheet also provides increased flexibility from >US$5.5 billion of liquidity and an investment-grade credit rating that enables self-funding of development projects. Annual sustaining pre-tax merger synergies has been guided at US$110–125m pa (2022: US$122m).
- **Focused on capital management.** In December 2022, Santos increased its on market buyback by US$350m. Capital management is based on at least a 40% payout of FCF from operations (excludes major growth) per annum. Santos Board will give further consideration to additional returns from asset divestments. Once Barossa and Pikka Phase 1 commence production, the Board intends to consider increasing returns to at least 50% of FCF. We see strong potential for capital management initiatives, particularly after the sale of 5% of PNG LNG to Kumul Petroleum, and other potential asset equity sell-downs (e.g., Dorado).
- **Largest acreage holder and producer of hydrocarbons in PNG.** Santos has the largest equity exposure to the long-life Exxon Mobil operated PNG LNG project (STO: 42.5% reducing to 37.5%) and has agreed to sell 5% of PNG LNG to Kumul Petroleum for net proceeds of US$1.1bn). We expect this transaction to settle in 1H 2023 (Kumul exclusivity period runs to 30 April). Santos has 22.8% equity (pre Government back-in) in the proposed Papua LNG project. We see a Papua four mini LNG train downstream development offering potential to deliver a material capex savings on the prior two LNG production train project design. TotalEnergies (upstream operator) has begun Papua LNG upstream engineering and design and plans to include CCS at the Elk field.
- **One of Australia's largest LNG suppliers to Asia.** Santos LNG portfolio (PNG LNG, DLNG, GLNG, and proposed Papua LNG) provides attractive LT cash flows, with a balance of oil-linked contracts and Asian spot JKM LNG pricing. The Barossa project provides new backfill gas that materially extends the life of the Darwin LNG plant, with first production expected in 2025 despite an environmental challenge that has suspended drilling activities. The Papua LNG joint venture has committed to a fully

integrated front-end engineering and design (FEED) process, and following the conclusion of this work by end 2023 / early 2024, the project is expected to be FID-ready. The Papua joint venture is targeting start-up by the end of 2027 / early 2028.

- **Two major oil developments in progress.** The Pikka Alaska oil project (STO 51% and operator) reached FID in August 2022, with project drilling planned to commence in 2Q 2023 and modular facility construction in 1H 2023. Santos is targeting first Pikka oil in 2026 at an expected production rate of 80,000 bopd gross, and opex of US$150m gross pa. The Alaskan gross 2C oil resource is substantial at 936 mmbbls, implying strong potential for further project expansion. The Dorado integrated oil and gas development (STO 70% and operator) offshore Western Australia has achieved regulatory approval and is targeting to be FID ready in 2023/24. Santos has forecast initial Dorado oil production of ~100,000 bopd (gross) and operating costs of <US$5/bbl.
- **A leading global CCS developer.** Moomba CCS Phase 1 is a low-cost 1.7 mmtpa CO 2 storage project in the Cooper Basin with capex estimated at ~US$165 million gross and a full life-cycle cost <A$30/t CO 2. Moomba CCS is expected to achieve first gas injection in 2024. Bayu-Undan CCS plans to capture Barossa CO2 and FEED is now complete, with Santos engaged on delivering regulatory and commercial frameworks. Santos has executed Bayu-Undan CCS MOUs with three potential customers for the maximum sequestration capacity of 10 mtCO2pa.

Shell PLC (SHEL)

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- **Advantaged portfolio.** In our view, Shell has three franchise businesses within the group, all of which are No. 1 in their respective areas. We believe global deepwater, integrated gas, and marketing form Shell's key competitive advantages. Shell's marketing business in particular generates >20% ROACEs consistently and is the highest-return business within the group.
- **Substantial free cash flow.** On our bullish commodity price deck, Shell's advantaged portfolio generates significant amounts of cash, supported by the company's oil leverage and No. 1 LNG presence. This leaves it well positioned to deleverage meaningfully over the coming years with cash to spare for higher shareholder returns.
- **Closing the gap.** On our estimates, Shell generates an FCF yield ahead of the sector on average over 2023E–25E but trades at a discount to peers on a DACF multiple basis. We think increasing shareholder returns should help to drive a re-rating versus peers, while continued de-leveraging sets up Shell to become a more stable business through the cycle.

SLB (SLB)
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- **Leading size, scale, geographic reach.** SLB's size, scale, geographic diversification, and exposure to new energy sources leave it favorably positioned under prevailing industry trends, in our view. We believe SLB is well positioned to benefit from the next leg of growth in International markets. International short- and longer-cycle investment is increasing, led by Latin America, the Middle East, and key offshore basins.
- **Digital evolution to drive financial results.** Growing contribution from the Digital and Integration business line should drive margin accretion over time. Integrated digital platform adoption also improves revenue stability and provides competitive advantage as the E&P industry increasingly embraces efficiencies. Over time, we believe the reduced capital intensity should drive improvement in the company's financial metrics.
- **International upcycle: less nascent.** SLB is well positioned to benefit from the next leg of growth in International markets. In 4Q22, SLB's y/y North American revenue increased 27% while International grew 26%, led by Middle East and offshore. The company noted that the Middle East is set to lead growth, with this cycle characterized by the region's plans to add oil and gas productive capacity.
- **Potential for long-term valuation accretion.** We believe SLB's exposure to a large addressable New Energy market should drive accretion to its valuation multiples over time. Key target markets include carbon capture, hydrogen, geothermal, critical minerals, and energy storage.
- See our latest SLB note here.

Suncor Energy Inc. (SU)
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- **New leadership in place.** On February 21, Suncor announced Rich Kruger as its new President and CEO. The new leadership change will be effective as of April 3, 2023. We know Rich well from his days at Imperial Oil and we are pleased that Kris Smith will remain in a leadership role with Suncor as he plans to take the reins as CFO, laying a clear CEO succession path in our view. We are also pleased that current CFO Alister Cowan will remain until the end of 2023 to ensure a smooth transition.
- **Unlocking higher shareholder returns.** Suncor anticipates that it will achieve the lower end of its $12–15 billion net debt target by the end of the first-quarter of 2023, opening the door to bigger shareholder returns. Indeed, the company's allocation of excess funds to buybacks should increase from 50% currently to 75%, with the balance earmarked for ongoing debt reduction. As of December 31, 2022, Suncor's net debt (company definition) stood at $13.6 billion (including $2.7 billion of lease liabilities).
- **Strong free cash flow profile.** We peg Suncor's free cash flow (before dividends and working capital movements and including A&D and capitalized interest) at $13.6 billion in 2023 under our base outlook (US$92 WTI, US$32.50 NYH 3-2-1). Our outlook factors in a refining & marketing (pre-tax) FFO of $6.4 billion in 2023. Under upstream futures pricing in 2023 (US$72 WTI), we peg Suncor's free cash flow at $10.7 billion.

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- **Adding value through sector consolidation.** Management continues to see attractive propane acquisition opportunities, and we expect the company to continue executing on acquisitions. In general, management targets deploying $200–300 million (lower in 2023 due to the pending Certarus acquisition) in capital per year and has been able to realize synergies that improve the EBITDA of acquired assets by ~25%+.
- **Strategic acquisition expands business into CNG/RNG/H2.** The pending $1.05 billion Certarus acquisition (expected Q2/23 close) ticks many of the boxes with respect to having a strategic and complementary fit (reduces seasonality and provides opportunities to cross-sell propane), is double-digit accretive to distributable cash flow per share, and has a strong organic growth profile, while also reducing the company's leverage. We expect the business to meet or exceed management's expectations in Q1/23. Please click here for our note covering the transaction.
- **Limited downside from a recession.** Weather is a much larger driver for the financial results compared to economic activity (a warm Q1/23 could be a near-term headwind). The company's U.S. operations (contributes ~45% of EBITDA, including the pending acquisition of Certarus) mostly serves residential customers, where propane consumption is driven by heating needs. We also note that the company tends to earn higher margins from residential customers, so it could benefit from a declining propane price (lag in pass-through) and a higher U.S. dollar. The company has also completed a number of acquisitions and we expect realized synergies to be a tailwind in 2023.
- **Potential take-private transaction.** Two investors accumulated a ~30% stake in SPB in 2020/21 on a diluted basis (Brookfield Asset Management and Marquard & Bahls). We believe that the combination of a weak share price and a somewhat capital-constrained growth profile (keeping debt to EBTIDA within management's 3.5–4.0x target) increases the chances of a take-private transaction.

Capital Markets

Tamarack Valley Energy (TVE)
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- **Top Clearwater producer with capacity to grow.** Tamarack's acquisition of Deltastream Energy has repositioned the company as the leading Clearwater producer with 734 net sections across the fairway. Management's 2023 Clearwater guidance points to 37,000 boe/d with $125–140 million in E&D capital budgeted to drill 69 net wells. The company highlighted more than 500 locations acquired in the Deltastream transaction and now estimates more than 200 Tier 1 and 2 Clearwater locations within the broader portfolio. We note that Tamarack is now the largest Clearwater producer by volumes (note here).
- **Return-of-capital framework well defined.** Tamarack increased its monthly dividend by 20%/25% following its Rolling Hills Energy acquisition and latest Deltastream Energy acquisition. The company remains committed to providing shareholder returns with 25%/50%/75% of excess funds flow to be directed toward its NCIB (note here) and/or special dividends as management reaches net debt target ranges of $900–1,100 billion, $500–900 million, and $500 million, respectively. The $500 million debt floor maps to roughly 1.0x D/CF at US$45/bbl WTI.
- **Strong corporate sustainability profile underscores robust FCF profile.** Recent M&A activity has shifted the corporate break-even to roughly US$37/bbl, with the Clearwater and Charlie Lake among the lowest breakeven plays in North America (note here). Management's 2023 guidance maintains 68,000–72,000 boe/d of production with a $425–475 million capital program; Tamarack highlights that a 1% reduction in the decline rate maps to a $10–15 million reduction in maintenance capital. In the company's five-year plan, management outlined a sustaining capital target of 50–55% of adjusted funds flow.
- **Strong balance sheet able to support further M&A.** Based on our updated estimates, we forecast Tamarack to carry approximately $932/$471 million in net debt at year-end 2023E/24E, representing a 2023E/2024E D/CF ratio of 0.9x/0.4x compared to most oil-weighted peers reaching a net cash position in 2023E. We do not model incremental M&A, though we believe this will be evaluated once net debt falls below $900 million per the company's updated return of capital framework.

Targa Resources Corp. (TRGP)

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- **Best way to play Permian and commodity upside.** Among midstream, we think TRGP will correlate best to constructive commodity tape into 2023. We like TRGP's top-tier platform in the Permian, coupled with integration to the docks on the Gulf Coast.
- **Growth projects.** TRGP has announced numerous organic growth projects that are expected to supplement and grow its cash flow. These projects include multiple processing plants in the Permian, Train 9 fractionator in Mont Belvieu under construction and Train 10 now permitted, and the Daytona NGL pipeline (twinning of the west leg of Grand Prix) that will support NGL volume growth from the Permian G&P assets and new plants under construction.
- **Financial flexibility.** Maintaining its healthy investment-grade balance sheet is a key focus point for TRGP when making decisions. Flexibility has improved, as leverage is trending lower and the structure simplification (DevCo repurchase and redemption of outstanding Series A Preferreds) has allowed for more impactful progress. This flexibility enables TRGP to continue investing in organic growth projects while returning meaningful capital to shareholders.
- **M&A.** TRGP contributed to some midstream consolidation during 2022 with multiple acquisitions. In July 2022, TRGP completed its acquisition of Lucid Energy's Permian Delaware Basin G&P assets for $3.55B (TRGP estimates a 2023E EBITDA multiple of 7.5x), which include 1,050 miles of natural gas pipelines and 1.4 Bcf/d of processing capacity in New Mexico. TRGP also acquired South TX assets from Southcross that have performed as expected and were an ideal acquisition given the stickier volumes provided from gathering to the wellhead. M&A will remain a part of TRGP's strategy, with location and potential for immediate synergies being the key, but it is not needed for the company to experience growth.
- **FCF and capital allocation.** Outlook for FCF is solid at our price deck, as we expect that TRGP can generate >$1B of FCF in 2024 even with ~$50mm/quarter of estimated stock buybacks through 2024 and another step-up in the dividend to $2.40/share, which should allow for debt leverage (post Lucid) to be back below 3x. In addition to debt reduction, TRGP will have many options for usage of the FCF including: (i) additional dividend growth; (ii) additional common stock buybacks; and (iii) higher capex.

Topaz Energy (TPZ)
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- **Diversified royalty model with a natural gas tilt.** Topaz's 2023E/24E production profile remains 70%/69% gas-weighted. Topaz is supported by some of the top operators in the WCSB. Notably, Tourmaline Oil has outlined a 5-year plan in NEBC Montney that is estimated to increase Topaz's regional volumes from 6,800 boe/d in 2022 to more than 10,000 boe/d by 2028. Topaz's latest acquisition, Deltastream (note here), has positioned the company as a top Clearwater royalty producer, now holding 52% of pro-forma OOIP at Marten Hills and Nipisi. Management now anticipates averaging 2,850 bbl/d of total Clearwater production in 2023, exceeding 3,000 bbl/d by 2024E. The royalty business model is insulated from industry cost inflation, providing margin stability.
- **Resilient infrastructure model.** Topaz holds working interests in five facilities backed by long-term take-or-pay commitments, a contracted interest in a portion of Tourmaline's third-party revenues, and a 49.5% interest in two water-handling facilities. The company's infrastructure portfolio is currently expected to generate 2023E revenues of $65 million and FCF $55 million, covering 38% of the 2023E dividend. Growth in the Infrastructure portfolio remains an area of focus as management continues to target a long-term 50-50 EBITDA split between the infrastructure and royalty business. As a result, we expect management to continue evaluating infrastructure M&A opportunities to expand the portfolio.
- **FCF allocation balanced between RoC and debt reduction.** Topaz increased its annual dividend to $1.20/sh (~6% dividend yield) with the latest Deltastream acquisition; we estimate a 49%/43% effective payout ratio in 2023E/24E. The company is able to balance its RoC program with continued deleveraging efforts, with our model pointing toward roughly $45 million in quarterly post-dividend FCF, on average, through 2023.

Tourmaline Oil (TOU)
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- **Natural gas weakness provides buying opportunity.** Weaker natural gas prices provide a buying opportunity for the Western Canada Sedimentary Basin (WCSB) natural gas producer that is returning meaningful capital to shareholders plus still growing modestly (+7%/year CAGR in the current plan), while being mindful that basin growth much beyond this figure could start to drive egress constraints.
- **Cheniere export agreement a well-timed deal.** We estimate US$1 increase in JKM pricing to result in roughly C$50–55 mm of incremental after tax cash flow in 2023. TOU has hedged approximately 10% of the JKM volumes at an average price of ~US$23/mmbtu, and we would expect the company to take advantage of the current strength by layering on additional hedges at even more attractive prices. See our note here.
- **Return of capital, with a vast majority of FCF to be returned.** TOU announced special dividends for Q1/23, with $2.00/sh payable on February 1. Our outlook now calls for two base dividend increases in 2023 (to $1.16/share annualized) on top of $2/sh specials in each of the quarters in 2023. As of March 2 on strip pricing, TOU is expected to generate $1.6–1.8bn in FCF in 2023 (or about $2.9bn at the RBC Deck). (see more here).
- **High-quality asset base, with North Montney driving the growth.** TOU's 5-year plan now includes development of its Northern Montney asset, Conroy, pushing corporate volumes to 700,000 boe/d by 2028. TOU expects Conroy to grow to ~100,000 boe/d in two tranches, with on-stream dates of 2026 and 2028 (set to coincide with the startup of LNG Canada). The plan incorporates capex spend of roughly half of forecast cash flows, leaving meaningful capacity for RoC programs. TOU remains well situated as it relates to LNG exposure in NE BC, a topic that we explored in recent reports here (1,2,3,4).

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- We do not make provisions for taxes and/or trading commissions when adding or removing stocks from the portfolio.

Note: Total return data for the list as well as relevant indices are from Bloomberg and FactSet.

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Companies mentioned

Hunting PLC (LSE: HTG LN; GBp236.00; Outperform)

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