Why Suncor Energy Inc. Thinks Oil Will Double In 3-4 Years

Description

While speaking at a CIBC conference in British Columbia, **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) CFO Alister Cowan expressed some optimism for oil prices. As he said on Wednesday, “In the longer term, oil is going to go back to $90-$100.” By “longer term”, he meant “probably in three years or four years’ time.” CEO Steve Williams has made similar pronouncements in recent months.

Mr. Cowan’s bold prediction was also a way of defending some of Suncor’s more questionable investment decisions. Most notable is the Fort Hills project, which has marginal economics even at higher oil prices, but is being developed by Suncor anyways.

So can we believe Mr. Cowan? And should we be buying Suncor shares? Below we take a look.

Why oil prices can rebound

Let’s be clear. No one is predicting an immediate price rebound. But over the longer term, there are reasons for Suncor to be optimistic.

It all goes back to classic supply and demand. With such low oil prices, producers will cut back on output, decreasing supply. Meanwhile, lower prices will help boost demand. And in the longer run, prices should adjust accordingly.

And we’ve already seen producers cut investment spending dramatically. Suncor is just one example, having recently cut another $1 billion from its 2015 capital budget (along with 1,000 jobs).

Why this will not happen any time soon

At the same conference, **Canadian Natural Resources Ltd.** (TSX:CNQ)(NYSE:CNQ) CFO Corey Bieber had a more pessimistic tone: “Are we going back to $100 oil? Not currently (in) our view. Are we going back to $60-$65 oil? That has some potential.” Suncor’s former CEO Rick George also sounded a pessimistic tone, saying that Canadian producers will maintain supply even if oil goes down to $30 per barrel. So who is correct in this debate?

Only time will tell. But I would not be as optimistic as Mr. Cowan.

In fact, Mr. Cowan's speech had an odd irony. He was predicting how supply would adjust (i.e., fall) in response to lower prices, but at the same time, he was defending Suncor's decision to press ahead with projects like Fort Hills. As he said in his speech, "You don't want to cancel or delay big projects in the middle." Why is he expecting other producers to act any differently?

Personally, I would argue that Fort Hills should be one of the first projects axed. Numerous analysts agree that it is one of the higher cost projects out there. And Suncor has said that Fort Hills has a 13% return on investment with oil at US$95 per barrel. Those numbers just aren't good enough in today's environment.

It may be time to sell Suncor

This is especially worrying. Suncor is supposed to be a financially disciplined company, but Mr. Cowan's remarks signal the company is unprepared for lower oil prices. CNRL may be a better option at this point, if for no other reason it seems better prepared for what lies ahead.

There's another energy company that should be on your watch list, and it's also The Motley Fool's top stock pick for 2015. You can read about it in the free report below.

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