Why Energy Investors Need to Pay Close Attention to Suncor Energy Inc.'s Earnings

Description

This week a slew of energy companies report quarterly earnings, giving us a chance to see how these companies have coped with low oil prices. One of these companies was **Suncor Energy Inc.** (TSX:SU)(NYSE:SU), which reported its results Wednesday evening.

So, how is Suncor coping with low oil prices? More importantly, what do these results mean for the industry? And finally, how should you react as an investor?

Not so bad

At first glance, Suncor's results look terrible. The company posted a net loss of $0.24 per common share, down from $1.01 per share in Q1 2014. Low oil prices were, of course, the main culprit—the American oil price averaged US$48.65 this quarter, down more than 50% year over year.

Yet beneath the surface, Suncor seems to be coping just fine. Cash flow from operations totaled $1.5 billion (or more than $1 per share), and exceeded capital expenditures. This was mainly caused by declining expenses—oil sands cash operating costs per barrel fell by 20% year over year and are now below $30.

Better yet, Suncor's production is still strong, having increased by 12% year over year in its oil sands operations.

What does this mean for the industry?

First, let's make one point clear: Suncor is not alone. All across the industry, oil companies have been able to reduce costs and continue to generate cash with such low oil prices. And the news only gets better from here now that oil prices have reached nearly US$60.

That’s the good news. But here’s the bad news: with so many companies surviving so easily, there’s not much upside for oil prices. Instead, I expect supply to easily keep up with demand for the timebeing.

How should investors react?

Unfortunately for investors, energy stocks remain quite expensive and are pricing in a big oil rebound. Suncor is a perfect example.

If you don’t believe me, just look at what Suncor’s stock price has done since the end of 2013: it’s gone up by 7%! Keep in mind that oil prices have gone from nearly US$100 to less than US$60 over this time. Investors clearly see low oil prices as just a blip.

But here’s the problem: oil prices could stay at this level for a long time. And if this happens, there’s clearly a lot of downside from current stock prices. So, at this point, I would hold off on buying energy stocks such as Suncor. There are much better options available.

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