3 Reasons to Hold Suncor Energy Inc.

Description

Energy investors continue to watch in horror as the rout in the oil patch decimates the valuations of many of the sector's former stars.

When the dust finally settles some names will disappear and others will simply emerge bigger and stronger than they were before the crisis hit.

Suncor Energy Inc. (TSX:SU)(NYSE:SU) will be one of the winners. The stock is holding up much better than most of its peers and conservative investors with a bullish view on the energy space should consider the company as one of their first picks when evaluating new positions in the patch.

Here's why:

Integrated business model

Suncor is Canada's largest integrated energy company, and its diversification, along the hydrocarbon value chain from production to retail, gives investors revenue stability during rocky commodity markets.

On the production or "upstream" side of the business, Suncor is primarily an oil sands producer. In fact, 6.9 of the company's 7.7 billion barrels of reserves and 18.8 of the total 23.2 billion barrels of contingent resources are located in its oil sands properties.

That's a lot of oil and it is all located in one spot, which means Suncor doesn't have to deploy billions of dollars buying land and drilling for new reserves. All the capital outlays can go towards making the production process as efficient as possible.

As an example, Suncor reduced its Q1 year-over-year operating costs per barrel by 20% to just $28.40.

Suncor also operates four refineries with a combined capacity of 460,000 barrels per day. These facilities take the feedstock crude oil and turn it into end products such as diesel fuel, lubricating oil, gasoline, and asphalt. Low input costs can boost margins in the refining division when crack spreads widen, and this helps offset weakness in the upstream operations.

The company's retail division includes more than 1,500 Petro-Canada service stations. Low gasoline prices tend to encourage drivers to take more trips and buy bigger cars. This all translates into more revenue for Suncor.

Strong balance sheet

Energy companies with high debt levels are getting killed right now because they aren't generating enough cash flow to cover all their obligations. Suncor doesn't have that problem.

The company finished Q1 with nearly $5 billion in cash and cash equivalents and just $13 billion in long-term debt, which is small for a company that has a market capitalization of $50 billion.

This puts Suncor in a very enviable position because it has the capability to ride out a prolonged slump in the market and has the firepower to gobble up prized assets as they come on the market at fire-sale prices.

Dividend growth and share buybacks

Suncor has a strong history of rewarding shareholders with increased dividends and an aggressive share-repurchase program. The distribution currently yields 3% and is one of the safest payouts in the sector.

Should you buy Suncor?

Some analysts say the stock is too expensive and that investors can get more bang for their buck by buying names that have been hit harder by the slump. That might be true, but there is also a lot more risk that comes with investing in struggling producers.

If you are a long-term bull on the oil sector, but you don't want to be worried about violent swings in stock prices, Suncor is a name you can simply buy and forget about for a couple of decades, and receive a nice 3% yield along the way.

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1. Energy Stocks
2. Investing

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