



How Would \$20 Oil Impact Suncor Energy Inc.?

Description

The latest forecast for oil prices suggests crude could drop all the way down to \$20 per barrel. That has far-reaching, negative implications for most Canadian producers, but a select few could actually benefit.

Let's take a look at **Suncor Energy Inc.** ([TSX:SU](#))([NYSE:SU](#)) to see what \$20 oil would mean for Canada's largest integrated energy company.

Upstream pain

Suncor's oil sands operations would certainly take a hit if oil dropped another 50%, but the company is in much better shape than many of its peers.

Production continues to increase, up 45,000 barrels per day in Q2 compared with the same period last year. Meanwhile, costs are dropping significantly. In fact, Suncor managed to get its operating expenses down to \$28 per barrel in the second quarter.

A plunge to \$20 would probably be short-lived, and Suncor is more than capable of riding out further weakness.

Midstream and downstream gain

The production side of the business gets most of the media attention, but investors should be focusing on Suncor's four large refineries and its network of 1,500 Petro-Canada retail outlets.

The refineries take crude feed stock and turn it into a variety of products including gasoline, diesel fuel, lubricants, and asphalt. The lower oil goes, the cheaper the input costs are for these facilities.

In the next year, those cost are likely to come down even further for Suncor's Montreal operations because the company will be able to send western Canadian crude through the Line 9 pipeline that is being reversed to carry the crude feed stock. The pipeline reversal has been heavily delayed, but should finally be in service by the middle of next year.

Low oil prices translate into lower gasoline prices and that tends to encourage people to drive more as well as buy larger vehicles. This is a benefit for Suncor's gas stations.

The integrated model really showed its strength in the most recent quarter. Suncor delivered operating earnings of \$906 million, of which \$631 million came from the refining and marketing (retail) units.

Acquisition potential

Suncor is sitting on more than \$5 billion in cash, and CEO Steve Williams recently said he is looking for opportunities to buy distressed assets at fire-sale prices.

If oil does actually plunge to \$20, many of the highly leveraged, high-cost producers are going to sell properties as they struggle to survive. Williams is willing to wait. He said the gap is starting to narrow between the price companies want for their properties and the price he is willing to pay.

Should you buy Suncor?

The company's rock-solid balance sheet and diversified business model puts it in a unique position to benefit from further weakness in the oil market.

If you are a long-term oil bull, Suncor is a solid holding, and you can collect a safe 3.4% dividend while you wait for better times.

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