Should Dividend Investors Buy Suncor Energy Inc. or Canadian Natural Resources Limited?

Description

Canadian oil and gas companies continue to struggle with low energy prices, and investors are wondering if the stronger players still offer safe dividends.

Let's take a look at **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) and **Canadian Natural Resources Limited** (TSX:CNQ)(NYSE:CNQ) to see how things are shaping up.

Suncor

The company is primarily known as an oil sands producer, but Suncor also operates large refining and retail divisions. The integrated model has served the company well during the downturn, and investors have been spared the massive haircut that has befallen the shares of Suncor's peers.

This doesn't mean that Suncor's upstream operations are not hurting, but the company is doing a good job of reducing costs while increasing output.

In Q2 2015, oil sands production increased by 45,000 barrels per day (bbl/d) compared with Q2 2014 and operating expenses dropped to $28/bbl.

On the refining and retail side, things are looking good. Suncor's four large refineries convert crude oil feed stock into finished products such as diesel fuel, gasoline, asphalt, and lubricants. With such low input costs, there is an opportunity to turn big margins on the processed products, especially when the spread widens between the WTI-based input cost and the Brent-based price of the finished goods.

Suncor also operates about 1,500 Petro-Canada retail locations. When gasoline prices drop, people tend to drive more, and that is good news for Suncor's bottom line.

Suncor surprised the market with a dividend hike when it reported Q2 earnings. The company raised the quarterly payout by a penny to $0.29 per share. That's good for a yield of 3.3%.

Operating earnings for Q2 came in at $906 million. The refining and marketing divisions accounted for nearly 70% of the profits.

Canadian Natural Resources

Canadian Natural Resources owns a diversified portfolio of oil sands, heavy oil, light oil, natural gas, and natural gas liquids properties located across Canada and overseas.

The company tends to control 100% of its assets, and this provides management with a lot of flexibility to move capital quickly when opportunities arise in various parts of the portfolio.

At the moment, Canadian Natural Resources is struggling with low prices in both the oil and natural gas markets.

In the second quarter of 2015, the company reported a loss of $579 million. The executive team blamed the poor result on the Alberta government’s 20% tax hike, but there are other concerns that investors should be focused on.

Canadian Natural Resources had Q2 operating cash flow of $1.5 billion, which was adequate to cover the $1.3 billion in capital expenditures, but the company also paid out $503 million in dividends. That means there was a cash flow shortfall of $300 million for the quarter.

Oil and gas prices have dropped significantly since the end of Q2, so the third-quarter numbers could be ugly. If that’s how things pan out, investors should prepare for a dividend reduction.

Should you buy?

Both companies are capable of riding out the rout, but Suncor’s integrated model is much more attractive in the current environment, and the dividend looks safe.

If you think oil and gas prices are headed higher, Canadian Natural Resources probably offers more upside potential, but I would stick with Suncor until the energy market is clearly on the mend.

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