



## When Will Suncor Energy Inc. Stop Burning Cash?

### Description

Excess cash flow has been tough to come by in recent years for **Suncor Energy Inc.** ([TSX:SU](#))([NYSE:SU](#)). Since 2012 incoming cash flows have barely covered ongoing capital expenditures needs, if at all. To cover the deficit, Suncor has been taking on increasing amounts of debt. Today, long-term debt stands at roughly \$15 billion, up from just \$9 billion in 2012.

Recently, **Moody's Corporation** downgraded the company, citing "the impact of low oil prices on Suncor's cash flow and leverage metrics."

Can Suncor turn things around?

Image of cash flow type unknown  
*Image Source: YCharts*

### A tough place to be

Most people point to Suncor's low production costs to corroborate the thesis that its assets are high quality. If you do a little digging, however, the idea that Suncor is a conservatively positioned producer just doesn't hold up.

In 2011 cash operating costs were roughly \$39 a barrel. That's gone on to fall every year since to just \$28 a barrel. Good news right? Unfortunately, a significant amount of production comes from oil sands projects, which not only have had persistent operating cost overruns, but also sell production at a discount to prevailing market rates.

For example, last month oils sands bitumen traded for as low as \$10 a barrel at a time when Brent crude was around \$30. That differential is a big reason why Suncor was only generating consistent free cash flow with oil prices above \$100 a barrel. When Brent fell to just \$60, Suncor started generating negative free cash flow. So while other analysts might tout Suncor as a low breakeven business, it likely needs something close to \$60 oil to be sustainable.

Screen Shot of cash flow type unknown  
Screen Shot 2016-03-08 at 2.16.26 PM

*Image Source: Suncor Corporate Presentation*

## Going all in

Last month, Suncor all but completed its multi-billion takeover of **Canadian Oil Sands Ltd.** Both companies were major partners in one of the world's biggest oil sands projects, Syncrude. Suncor's 12% interest in that project will jump to 49% after the deal is completed. While Syncrude is largely to blame for Suncor's past troubles, management seems to be going all in on the deal.

The acquisition brings on some major risks for Suncor. Moody's downgraded Canadian Oil Sands's credit rating recently, citing its "very high cost base" and "high leverage." It was the first large Canadian oil producer to receive a junk rating in at least a decade. If oil prices can't sustain a rebound over \$50 a barrel in the next year or two, the deal has a fairly good chance of being a dud.

Fortunately, Suncor can rely on its diversified business model to keep it afloat until oil rebounds. Its refining business, which typically increases its profits when oil falls, posted earnings last year of \$2.2 billion, more than offsetting the \$111 million operating loss in its oil sands business.

The company remains one of North America's largest refiners with the capacity to process nearly 500,000 barrels of crude per day. It's likely the refinery arm that's attracted big-time investors like Warren Buffett, who owns over \$1 billion in Suncor shares.

While the Canadian Oil Sands acquisition brings some production risks, Suncor will have no issue surviving due to its refinery arm. If you're unsure if oil will continue rebounding this year, however, investing in a major oil sands producer like Suncor may not be the safest place. It seems like Suncor is only best suited for long-term investors as many of its major producing assets may take years to turn a respectable profit.

## CATEGORY

1. Energy Stocks
2. Investing

## TICKERS GLOBAL

1. NYSE:SU (Suncor Energy Inc.)
2. TSX:SU (Suncor Energy Inc.)

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