Is Suncor Energy Inc. a Smart Play?

Description

If investors have been holding their oil stocks through this long downturn in the price of crude, professionals need to rethink their criticism of retail investors because that took a lot of courage. I've avoided the oil markets almost entirely for the past couple of months because I couldn't predict where the price of oil was going and was uncertain about when the sector would turn around.

However, one company that I believe investors should be paying attention to is **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) for a few reasons.

The primary reason has to do with the fact that it is one of the largest and most efficient oil suppliers in Canada. Unlike many of the other companies that took on significant debt, oftentimes 100% or more than their market cap, Suncor has been a bit more conservative. While its debt is $15 billion, that's only 34% of its market cap. Essentially, the company has taken on more debt as the price of oil has continued to go down.

But while debt always makes me nervous, because of the company's integrated business model, it's been able to continue generating revenue and driving future production growth. Consider that in 2015, the company only reduced its capital budget by 4%. This year it has bumped that up a little to 7%, but that's still nothing compared to the 40% in 2015 across the industry.

There are two drivers of this…

On its oil production side, it's a low-cost producer. In 2013 its total oil sands cash operating cost was $37.00 per barrel. That means it cost the company that much to get a barrel out of the ground. By 2014, it got that down to $33.80. And in 2015, that cost was $27.85.

The driver for this reduction in cost is a cut in operating expenses. In 2015, its operating expenses were cut by $900 million. However, because the company didn't cut back on its production like others, it saw an 11% oil sands production growth, which helped cut a few dollars from the cost per barrel.

In this environment, being able to save money on the oil coming out of the ground is key to the company surviving.

However, another reason why Suncor has been able to do so well is because of its oil refinery business. Despite oil prices dropping, last year its oil refinery business earned $2.2 billion. Believe it or not, when the price of oil drops, the amount of money a refiner can make improves. And because Suncor has the capacity to refine 500,000 barrels a day, it has been able to keep earnings up while oil remains down.

But because it recognizes that a complete dependence on fossil fuels could be dangerous, it has also been diversifying into the renewable energy sector. It has generated 287 MW of wind power in Alberta, Ontario, and Saskatchewan for the past decade. It has four more farms in production that will generate 440 MW. It also has three solar farm projects in early development, which should provide a total of 240 MW of solar power.

All told, Suncor is the smartest of the oil plays right now. It is secure, it generates significant earnings, and it is diversified across multiple business models. Therefore, if investors want to buy a stock to enjoy the oil rebound, Suncor would be the right one.

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