Why Suncor Energy Inc.'s Big Bet on Oil Sands Will Eventually Pay Off

Description

Canada's largest integrated oil company **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) has bet big on oil sands over the last year, spending $6 billion on acquisitions during that period. The rationale for those purchases has been quite simple: management has sought to take advantage of the distressed asset prices triggered by the prolonged slump in crude to beef up oil production and reserves.

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This ability to grow at a time when other energy companies are cutting expenditures, restructuring, and even facing bankruptcy makes Suncor stand out from the crowd. It's a stock that every investor should own.

Now what?

One of Suncor's greatest strengths has been its rock-solid balance sheet. In tandem with Suncor's refining and marketing operations, which experience greater profitability when oil prices are low, the strong balance sheet is one of the reasons why Suncor has weathered the prolonged slump in oil prices and is in remarkably good shape.

Nonetheless, what really makes Suncor stand out has been its exceptional ability to take advantage of distressed asset prices by making quality acquisitions at bargain-basement prices in order to boost oil reserves and output.

These include the addition of 77,000 barrels of daily oil production with the $4.2 Billion purchase of Canadian Oil Sands Ltd. Along with the purchase of **Murphy Oil Corp.'s** 5% stake in Syncrude, Suncor is the project's single largest owner. Management hopes these purchases will give it sufficient traction to drive operational changes, boost output, and reduce costs at one of the industry's most unreliable operations.

These acquisitions, however, have not come without some controversy; there are fears that Canada's oil sands will become stranded assets.

You see, there is considerable opposition to the extraction of crude from oil sands as doing so consumes up to five times more resources than conventional oil for every unit of energy produced. It's also responsible for up to 20% more greenhouse gas emissions than conventional oil operations.

Regardless of these growing environmental pressures, there remains a place for oil sands in the global energy mix because conventional oil and U.S. shale production are incapable of meeting the expected long-term growth in demand.

After all, the U.S. Energy Information Administration expects global demand for crude to grow by a massive 48% between now and 2040. This outlook is supported by estimates formulated by the International Energy Agency, or IEA. The IEA predicts that India will become a key driver of the growth in world demand for crude. The IEA also expects global oil markets to rebalance by 2020, causing oil to rise to US$80 per barrel, which will be beneficial for Suncor with its low cash costs and higher oil output.

More impressively, Suncor has recently completed a $2.5 billion equity raising that has allowed it to bolster its balance sheet and refresh its war chest, so it’s capable of making further opportunistic acquisitions.

As a result, there has been considerable conjecture that it may seek to expand its 51% stake in the Fort Hills oil sands project by acquiring further shares from project partners **Total S.A.** and **Teck Resources Ltd**. Industry insiders are also speculating that Suncor could be looking at growing its conventional offshore oil operations in eastern Canada, where it holds interests in all producing fields including Terra Nova, White Rose, and Hibernia.

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So what?

Suncor has approached the prolonged weakness in oil prices as a unique low-cost opportunity to bolster its oil reserves and significantly grow production. Suncor is well positioned to unlock for value for investors as the price of crude rises because of growing demand for oil.

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