1 Oil Sands Giant That's Poised to Soar

Description

The outlook for crude is growing more optimistic primarily because of Trump's decision to exit the nuclear deal with Iran, falling global oil inventories, and firmer demand growth. The threat of further supply disruptions because of tensions in the Middle East is also helping to buoy prices. Oil's long-awaited recovery, which saw West Texas Intermediate (WTI) briefly trade above US$70 per barrel for the first time since 2014 is a boon for Canada's energy patch.

One of the less risky bets on higher oil is energy major **Suncor Energy Inc.** (TSX:SU)(NYSE:SU), which has surged by 18% over the last three months and shows signs of rallying further still.

Now what?

Suncor reported some solid first quarter 2018 results, despite production declining by 5% year over year, thus highlighting the considerable strengths of its business. The drop in oil production can be attributed to a weather-related outage at its oil sands operations early in the quarter.

Clearly, that means Suncor's production should improve during the second quarter 2018.

Core to Suncor's ability to produce solid financial results lies in its ability to maintain a strong return on capital employed (ROCE) regardless of weaker oil prices. For the first quarter, it reported a ROCE of 6.5%, which was three full percentage points higher than the same period in 2017.

Suncor's refinery operations continue to fire on all cylinders. The energy giant reported the highest ever first quarter utilization rate and throughput of crude.

Meanwhile, the Fort Hills oil project achieved first oil production at the start of the quarter and ended the period with average output of 29,800 barrels daily. That production will continue to grow because operations are being ramped up ahead of schedule.

Fort Hills has the capacity to produce 194,000 barrels daily, making it one of the largest oil sands projects to come online recently. The asset has the ability to significantly boost Suncor's overall production, giving its bottom line a healthy lift, particularly in an operating environment in which oil is rising in value.

Suncor also expanded its interest in Syncrude Canada Ltd., acquiring **Mocal Energy Ltd.**'s 5% stake in the asset for US$730 million, adding around 17,500 barrels daily of synthetic sweet crude to its production and giving it a 59% interest in the operation. Production at the offshore Hebron project, where Suncor has a 21% interest alongside **Exxon Mobil Corporation** and **Chevron Corporation**, is continuing and will yield 30,000 barrels daily to Suncor when it peaks.

The integrated energy giant has forecast 2018 production of 740,000 to 780,000 barrels daily, representing an 8% to 14% increase over 2017. Such solid steady production growth will give Suncor's earnings a healthy boost, particularly in an operating environment where WTI remains firm and is trading at close to its highest price since late 2014.

Another important aspect to consider, especially with oil sands being responsible for 82% of Suncor's production, is that the differential between Canadian heavy oil known as Western Canadian Select (WCS) and WTI is closing.

It has already fallen from around US$30 per barrel at the end of last year to be just over $14, thereby helping to boost Suncor's profitability. That differential is expected to continue easing over the remainder of 2018 as increased pipeline capacity and crude by rail reduces the transportation constraints that caused it to blow out at the end of 2017.

So what?

Suncor remains a firm favourite for investors seeking a lower risk stock to boost their exposure to oil. Its integrated operations, which include oil production and refining as well as its diversified portfolio of assets spanning oil sands and conventional oil production, help to mitigate some of the risk associated with its operations.

Further, management's proven ability to maximize its return on capital and execute long-term projects that will boost reserves as well as production demonstrates that there is a long growth runway ahead. That bodes well for strong earnings growth and for its market value to appreciate.

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