



Boost Income and Growth by Adding Suncor Energy Inc. (TSX:SU) to Your Portfolio

Description

Oil [remains weak](#) despite a range of positive fundamental factors including additional supply constraints and firmer than anticipated demand growth. After being caught in a prolonged slump that has lasted for more than four years, sub US\$60 oil is appearing to be the new normal. While crude's latest volatility is deterring investment in the energy patch, Canadian integrated energy major **Suncor Energy Inc. (TSX:SU)(NYSE:SU)** remains an attractive investment that will benefit from oil's long-awaited recovery.

Quality refining operations

Unlike many of its peers and smaller upstream oil sands producer, the integrated energy major was able to profit from the [deep-discount](#) applied to Canadian heavy crude that reached a record of over US\$47 a barrel in late October 2018. This is because Suncor possesses considerable refining operations that are capable of processing over 68% of its total oil sands production based on its 2018 annual refinery throughput.

During 2018 Suncor's refining and marketing operations processed an average of almost 431,000 barrels daily, which, despite being 2% lower than 2017, saw that businesses net earnings expand by almost 19% to \$3.2 billion. The energy major also reported record refinery throughput of 467,9000 barrels daily for the fourth quarter 2018.

The strong annual earnings growth can be attributed to the wide differentials between Canadian heavy crude known as Western Canadian Select (WCS) and the North American benchmark West Texas Intermediate (WTI). These differentials meant that while feedstock for Suncor's refineries was cheaper, it could still obtain higher premium prices for the petroleum products produced. Suncor is therefore well equipped to manage the volatility associated with Canadian oil prices, and is not as significantly impacted by higher prices triggered by Edmonton's mandatory production cuts, making it uneconomic to ship crude by rail.

Growing oil production

The company's oil sands operations reported record production for the fourth quarter 2018 of 740,800 barrels daily and company wide average annual oil output of 732,000 barrels daily, which was 7% greater than 2017. Such strong production growth positions Suncor to fully benefit from higher oil prices and the narrow differentials between WCS and WTI.

Suncor's upstream oil operations have low cash costs, which means that even with WTI trading at around US\$55 per barrel, those operations are profitable, especially now that the differentials for WCS and Edmonton Par to WTI have narrowed significantly. For 2018, the energy major announced cash costs for its oil sands operations of \$25.25 per barrel produced, less than half of WCS's current market price of \$58 a barrel.

Low production costs combined with growing oil output and firmer prices, with many analysts tipping that WTI could rise to over US\$60 a barrel during the year mean that Suncor's earnings will grow. The company anticipates that cash flow between the end of 2018 and 2023 will have a 5% compound annual growth rate (CAGR), as a range of initiatives reduce bottlenecks and increase efficiencies at Suncor's operations.

Despite the solid operational performance, Suncor reported a fourth quarter net loss of \$280 million and that annual net earnings had fallen by 26% year over year to \$3.3 billion. The sharp decline in net income can be blamed on foreign exchange losses, a \$223 million impairment charge on Suncor's equity investment in **Canbriam Energy Inc.** and notable weaker oil over the final quarter of 2018.

The strength of Suncor's operations and its ability to grow production as well as generate considerable cash flow despite weaker crude means it is one of the few energy companies that didn't cut its dividend when the oil slump began.

In fact, the energy major hiked its quarterly dividend by 17% at the end of the fourth quarter to \$0.42 per share, which gives it a tasty forward dividend yield of almost 4%.

Why buy Suncor?

Suncor is an attractively valued and compelling play on higher oil. Not only can it insulate much of its cash flow growth from the volatility associated with oil because of its integrated operations, but its focus on driving efficiencies along with growing production will give earnings a healthy boost. These attributes make Suncor an appealing growth and income investment for every portfolio.

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