Is Suncor Energy (TSX:SU) the Next Exxon Mobil (NYSE:XOM)?

Description

Is **Suncor Energy** (TSX:SU)(NYSE:SU) the next **Exxon Mobil** (NYSE:XOM)? Well, it depends on what you mean. In many ways, Exxon has become the best-in-class oil company on the planet, armed with a $300 billion market cap. However, Exxon stock has returned *0%* over the last 13 years!

So, when we ask if Suncor is the next Exxon, it's important to narrow the question. Is Suncor set to increase in size by 500% and become an incredible capital allocator? Or will Suncor leave its shareholders stranded for the next 13 years? Let's find out.

Warren Buffett speaks

There's at least one famous investor who believes in Suncor: Warren Buffett of **Berkshire Hathaway**. Earlier this year, he purchased 10.8 million shares. Notably, he's owned shares before. In 2013, he purchased a sizable stake only to sell it in 2016 at breakeven prices. This familiarity with the company is likely what spurred his latest purchase.

In late 2018, Suncor shares slumped nearly 40% after pipeline bottlenecks forced regional oil prices to drop by as much as 70%. Every Canadian producer was crushed, including Suncor. Buffett swooped in nearly at the bottom. After Alberta instituted an emergency supply cut, regional prices rebounded quickly, sending Suncor stock up 30% in just a few months.

Apart from his familiarity with the company, what made Buffett pull the trigger on buying shares? He's likely excited about the company's integrated business model. That means that Suncor not only produces oil, but it also refines and transports the output to bring it to market. Being an integrated producer is a big advantage when oil prices are volatile. If you only produce oil, you benefit when selling prices rise. When prices fall, you feel the pain. By owning refineries, integrated producers can offset much of this pain, for when oil prices fall, refinery profitability often *rises*.

Because it owns enough refinery capacity to process nearly all of its output, Suncor can weatherstorms significantly better than many of its peers. A cratering share price and resilient business modellikely pushed Buffett over the edge. Just be careful — long term, this stock might be a dud.

Suncor is not Exxon

While Exxon hasn't made much money for investors recently, it does have a stellar long-term record. We're talking decades here, not just years. Since 1980, Exxon shares have returned more than 2,000%. And that's not even counting the dividend, which currently stands at 5.1%. Suncor hasn't done too badly over the decades either, but there's a big difference: Exxon is positioning its business for the next century, while Suncor seems set on just the next decade.

The only proof you need is in their exploration activities. Take a look at Exxon's recent discoveries. According to *Bloomberg*, Exxon "plans to reduce the cost of pumping oil in the Permian to about $15 a barrel, a level only seen in the giant oil fields of the Middle East." Staale Gjervik, who runs Exxon's shale division, thinks these projects "will become competitive with almost anywhere in the world."

Clearly, Exxon isn't betting on ever-higher oil prices to survive. Instead, it's focusing on reducing costs as much as possible. Suncor, however, has a much different future. Suncor's projects are heavily exposed to oil sands production. Because this production requires more refining to get to market, the output generally sells at a discount. Some of this discount is absorbed by Suncor's refining arm, but not completely. At the end of 2018, Suncor's management was targeting all-in breakeven costs of under US$50 per barrel. Compare that to Exxon's potential US$15 per barrel breakeven price in the U.S., and you start to understand the structural differences in each business.

Suncor stock may still rise in the coming years, but it won't be because it's like Exxon. In fact, shares could rise because the company *isn't* like Exxon. Higher breakeven prices mean slimmer margins when oil prices are low. If oil prices rise, Suncor's profitability would grow significantly faster than Exxon's. Just keep in mind that the opposite is also true — if oil prices fall, Suncor could be in trouble fast.

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