Warren Buffett Loves Suncor Energy (TSX:SU) for 1 Reason

Description

Warren Buffett loves **Suncor Energy** (TSX:SU)(NYSE:SU). Last year, his holding company **Berkshire Hathaway** reported a 10.8 million stake in the company. That puts Berkshire's ownership level close to 1%.

This isn't the first time he's purchased shares. Buffett bought shares back in 2013, though he sold the position in 2016.

To be sure, Canada's energy market is still feeling a lot of pain, but *Reuters* highlighted that Buffett's purchase "could revive investor interest in the languishing Canadian energy sector."

With a deep knowledge of Suncor's business model, Buffett is betting big that shares are undervalued. Should you follow this legendary guru?

Pay close attention

It's surprising to see Buffett enter the Canadian space. The entire sector is still dealing with pipeline capacity issues that sent local prices spiraling in 2018. Pipelines take years to build, so this issue won't be going away any time soon.

Additionally, Canadian output is notoriously lower quality, whether its from oil sands or heavy oil projects. This production requires more refining to bring to market, meaning higher costs, resulting in a sizable pricing discount.

Many investing gurus have stayed far away. Jeremy Grantham, co-founder of GMO Asset Management, a $100 billion investment manager based out of Boston, once called oil sands projects "stranded assets." That is, he thinks they'll ultimately provide investors with *zero* value.

What does Buffett see in Canada's beleaguered energy sector? Well, he may not see anything in the sector writ large, but there's certainly plenty to love for Suncor specifically.

What Buffett loves

Cavan Yie, a portfolio manager at **Manulife Financial**, laid out the investment case succinctly.

“Berkshire is typically a countercyclical value investor, so we are not surprised the interest was renewed in a name like Suncor,” he notes. “Suncor is somewhat insulated from these risks given the fact that they have a strong downstream operation, which financially benefits from oil bottlenecks and that is unique to Suncor, which you can’t get with many other companies in the energy space.”

What Yie is highlighting is Suncor’s integrated business model. Most oil producers are solely that: producers. They try to drill for as much oil as possible, as cheaply as possible. From there, it’s a pure commodity, fetching whatever price the market dictates. Apart from hedging, there isn’t much companies can do to avoid being at the whims of market fluctuations.

Suncor is a bit different. In addition to being an energy producer, it also owns its own refineries and pipelines. This is a major advantage. When oil prices fall, for example, refinery margins often rise. Owning both offsets volatility in either business.

Additionally, limited pipeline capacity is a driving force behind Canadian crude selling at a discount. By owning its own pipelines, Suncor doesn’t have to worry about capacity constraints or surprise price increases.

In a nutshell, by owning the entire value chain, Suncor controls its own destiny. You can’t say that about many Canadian energy companies. Buffett likely noticed that shares were brought down alongside the market-wide decline, the proverbial throwing the baby out with the bathwater. With his existing knowledge of the company, he was able to capitalize quickly, before prices revert higher.

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