OPEC Oil Deal: Should You Buy Suncor Energy (TSX:SU) Stock Today?

Description

Global oil producers just agreed to make the largest supply cut in history. Contrarian investors are now wondering if this is the right time to buy oil stocks.

OPEC deal

OPEC and its partners announced a plan to cut global oil supply by 9.7 million barrels per day (bpd). The consortium hopes to stabilize the industry and boost market prices.

What's the scoop?

Saudi Arabia and Russia are ending a price war that recently drove oil to lows not seen in nearly two decades. WTI fell to US$20 per barrel in March. It bounced as high as US$29 in the first week of April on hopes of a major supply cut, but the rally quickly faded. At the time of writing, WTI trades at US$23, roughly equal to its closing price last week before the new agreement.

The lack of a rally on the news could mean global traders are not impressed with the size of the cuts or don't believe OPEC and its partners will actually deliver on the promises. The reductions will begin May 1 and continue at 9.7 million bpd until the end of June. The cuts then drop down to 7.7 million bpd through the end of 2020. In January 2021, it will drop to 5.8 million bpd until the end of April 2022.

The group, which includes 23 oil-producing countries, will meet in June to assess the need for further action.

Current oil situation

Oil demand is off significantly due to the downturn in the global economy caused by the coronavirus pandemic. Storage facilities around the world are filling up quickly, and some analysts say WTI oil could drop to US$10 if more supply isn't taken off the market.

Suncor

Suncor Energy (TSX:SU)(NYSE:SU) is Canada's largest integrated energy company with production, refining, and retail operations.

The stock traded at $45 per share in January. It fell as low as $15 in March and currently sits at $22.50. The plunge from the 2020 high has wiped out $34.5 billion in Suncor's market capitalization.

Suncor recently raised $1.25 billion in cash through the bond market. The company had to offer a 5% coupon, which is higher than Suncor would normally pay but is still reasonable in the current market conditions. The company also increased its credit facilities by an additional $2.5 billion.

The moves help ensure the company has the liquidity needed to ride out the slump.

The Canadian government is working on various aid programs to help industries hit the hardest by the downturn. The energy sector might require $15-20 billion.

Suncor could take advantage of its strong position in the market to add new reserves and production at discounted prices. Management did this when oil crashed in 2014-2015, and it wouldn't be a surprise to see deals emerge in the next six to 12 months.

Suncor has a strong balance sheet, and the dividend should be safe in the near term. Investors who buy the stock today can pick up a yield of 8.25%.

Risks?

The stock price could retest the March low if the broader market dips again, or if global oil storage approaches capacity in May and the price of oil drops back below US$20.

The downstream businesses normally act as a solid revenue hedge for Suncor. However, demand is down for jet fuel, gasoline, and diesel fuel. People are not driving and planes are grounded.

The longer the lockdowns continue, the worse the impact will be on the refining and retail operations.

Should you buy Suncor stock?

Ongoing volatility should be expected. However, the share price appears cheap at this level. The dividend should be safe, unless the oil rout drags on much longer than anticipated.

Contrarian investors with a bullish outlook on a 2020-2021 recovery in the global economy might want to consider a small position in Suncor for a buy-and-hold portfolio.

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Date
2025/07/29
Date Created
2020/04/13
Author
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