Should You Buy Suncor Energy (TSX:SU) After its Steep Dividend Cut?

Description

It was a hard squeeze for energy companies recently amid the record-low oil prices. Energy demand has declined to notoriously low levels amid the pandemic-driven lockdowns in an already oversupplied market. The Canadian oil and gas giant **Suncor Energy** (TSX:SU)(NYSE:SU) was no exception and bore the brunt in the first quarter.

Suncor Energy's Q1 earnings

Suncor Energy's quarterly numbers realistically paint the current gloomy picture of the energy markets. The integrated energy titan reported a $3.5 billion loss in the first quarter against a profit of $1.2 billion in the year-ago period. The company yet again cut its capital spending from $4.2 billion to $3.8 billion for the current year. It also cut quarterly dividends by 55% to $0.21 per share.

This has largely been the trend in the energy industry in the last few months. As oil prices plunged to record-low levels, the companies are instigating methods like dividend cuts and reduced capital spending to retain cash.

The current levels of oil prices are hardly beneficial for anyone. No oil producer has a breakeven level close to these levels. Thus, lower crude oil prices for longer will make the case bleaker for these energy companies.

Suncor Energy's annualized dividend now comes around $0.84, implying a forward yield of 3.6%. That's a significant fall from close to 8% levels earlier. It did not cut dividends during the 2008 financial crisis, and thus, Suncor's steep payout cut this time might have come as a shock for many.

Dividend cut

However, the cut was expected and in line with the industry trends, hinting that the energy industry is in deep waters. The oil major **Shell** also trimmed its dividends by 65% last month — its first in the last 75 years.

The dividend cut is indeed disheartening for investors. However, it will make Suncor Energy better placed to weather the challenging times. The company will save approximately $800 million given the dividend cut and reduced capex. It will give the flexibility to sustain longer in the lower oil price environment.

Interestingly, crude oil prices have notably ticked higher this week. In the last six trading sessions, WTI crude oil has almost doubled, as major economies are planning to re-open. It's important to note that even if lockdown and travel restrictions are lifted, it will take time to get things back to normal. It also seems like we have seen oil's bottom and a big rally is in the making.

Suncor Energy and crude oil in the post-COVID period

That will be a big positive for oil companies, but things will not change for them overnight. The second-quarter earnings are also expected to be unpleasant given the relative magnitude of the closures. However, Suncor Energy's downstream operations will play a more vital role when oil consumption will rise in the post-COVID-19 period, particularly if oil prices remain low.

Suncor Energy's weak Q1 earnings and a dividend cut could push the stock further down. It has already lost around 45% so far this year.

However, long-term investors should not make their investment decisions on a couple of weak quarters. The company is fundamentally strong, and its balance sheet now looks even better positioned to survive the crisis. Thus, the momentary weakness in its stock could be a lucrative opportunity for long term investors.

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