Should You Rush to Buy Suncor (TSX:SU) Stock?

Description

So far, **Suncor Energy** (TSX:SU)(NYSE:SU) stock has corrected by about 44% this year. The unprecedented decline in demand amid the COVID-19 outbreak and supply glut took a toll on crude oil prices and pushed oil and gas companies into uncharted waters.

The considerable decline in Suncor's stock price must have caught your attention, especially if you are value investors. Further, the hopes of recovery in oil prices from the re-opening of the economy strengthen the bull case. But should you rush to buy Suncor stock now?

Uncertainty overhang

Suncor's integrated business model positions it well to benefit from the recovery in demand and mitigate some of the price volatility. Further, it is focusing on reducing operating costs to bring down the cash breakeven price. Suncor has suspended its share-repurchase program and has reduced its quarterly dividends by about 55% to $0.21 per share. Suncor has reduced its capex guidance by about $1.9 billion, or 33%, from its previous guidance. Moreover, it plans to cut operating costs by 10% when compared to the prior year.

The combined impact of these measures has resulted in lowering the cash breakeven price for the company to a WTI price of US$35 per barrel.

Besides reducing costs, Suncor is focusing on maximizing the price realizations by shifting its production and refining mix towards higher-priced light crude and higher-value distillate. Following the strategy, Suncor's synthetic crude oil production came in at 503,600 barrels per day in the most recent quarter. Suncor also maintains a strong balance sheet and has ample liquidity to weather any adverse economic environment. Further, the company has no debt maturities in 2020.

The cost-reduction measures and the company's financial health look reassuring. However, before you jump to buy Suncor stock, understand that the high degree of uncertainty surrounding the economy suggests otherwise.

Even if the demand gradually rises, it is highly uncertain at what pace the recovery might come. Moreover, the global crude inventories indicate that it is likely to take time before the demand/supply imbalance comes back to normal. The bigger problem is the lack of coordination between the OPEC nations, resulting in a negative impact on crude oil prices.

Now what?

Suncor, being one of the largest and trusted energy companies, is likely to recoup its losses. However, the pace of recovery is hard to gauge. Further, Suncor’s current valuation fails to appeal. Despite the steep decline in its stock price, Suncor stock trades at a higher valuation when compared to the industry average. Suncor is trading at next 12-month EV-to-EBITDA ratio of 10.2, which is significantly above the industry average of 2.1. Also, Suncor stock is trading at the next 12-month EV-to-sales ratio of 2.1, which is even higher than the industry average of 0.6.

The high level of uncertainty, reduction in yield following the dividend cut, and high valuation provide good reasons why shares of Suncor might not be the best investment choice at the current levels.

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