Should You Follow Warren Buffett and Invest $2,000 in Suncor (TSX:SU) Stock?

Description

Suncor Energy (TSX:SU)(NYSE:SU) stock is one of the biggest in Canada. Even after a coronavirus-related slide, the business still garners a $38 billion valuation.

It's not just sheer size that commands the market's attention. Last year, Warren Buffett scooped up 10.8 million shares — nearly 1% of the entire company. It was a big bet, with industry analysts lauding the move.

"Berkshire's investment puts the Buffett stamp on Suncor and could be seen as a positive for the Canadian energy sector," the *Financial Post* noted. "The move comes at a time when global investors have been pulling away from Canada because of its carbon-intensive oil sands and struggle to approve pipelines."

Reuters was even more bullish about Buffett's purchase, saying that it "could revive investor interest in the languishing Canadian energy sector."

Should you follow the Oracle of Omaha and buy Suncor stock?

Here are the facts

The first thing that you should know is that Buffett's purchase came at a higher price than the current trading range. His average price point was likely around $40. Today, Suncor stock is valued at just $25. What happened?

Buffett initially got involved at the start of 2019. The previous few months were extremely difficult for Canada's energy sector.

For years, Canada was plagued by a lack of pipeline infrastructure. Right before Buffett jumped in, these challenges came to a head. Pipelines were flooded by a surge of industry supply. Suddenly, there was no way for fossil fuel producers to ship their product. They *needed* to secure pipeline space to survive.

The result was a bidding war that saw regional oil prices slump by more than 70%. The U.S., meanwhile, had ample pipeline capacity, meaning oil prices there were barely impacted.

Most oil producers live and die by the price of oil. The entire industry sold off, including Suncor. But here's the thing: Suncor has a secret weapon that insulates it from falling oil prices. This secret weapon even protects it from limited pipeline capacity. It's for this reason that Buffett likely bought shares.

Suncor is ready

Suncor is what we call an *integrated* oil company. That means it controls the entire supply chain, including pipelines. The stock fell during the rout of 2018, but the company doesn't even rely on external pipelines. Controlling its own pipeline network is a big advantage in any market.

As an integrated oil company, Suncor also controls its own refineries. These are facilities that turn crude oil into usable products like kerosene and jet fuel. Refinery margins run counter-cyclical to oil prices, so when commodity prices *fall*, refinery profitability *rises*. It's yet another way Suncor insulates itself from the market's gyrations.

However, none of these advantages were a match for COVID-19, which has caused energy demand to plummet. An ongoing supply war has pushed pricing even lower.

Is now the time to follow Warren Buffett and buy a few thousand dollars of Suncor stock? That depends entirely on how long the coronavirus situation depresses demand.

Do you envision a return to normal in 2020 or even 2021? With its integrated business model, Suncor should survive the lean months ahead, taking advantage of lesser-financed competitors once conditions normalize.

If conditions remain atypical, however, even strong operators like Suncor will be in trouble. Most analysts think the company breaks even at US$40 per barrel. That means the company is currently racking up multi-million-dollar losses *daily*. It can only keep that up for so long.

If you have conviction that COVID-19's effects will wane within 12 months, a bet on Suncor stock may be prudent. But if you lack that conviction, stick to the sidelines.

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