Suncor Energy (TSX:SU): Should You Buy the Stock at $23?

Description

Suncor Energy (TSX:SU)(NYSE:SU) continues to trade at a depressed price and contrarian investors are wondering if this is the right time to buy the stock.

Let's take a look at the situation in the oil industry to see if Suncor deserves to be on your buy list right now.

Oil price outlook

Suncor is best known for its oil sands operations. The company also has offshore oil production and downstream assets that include refineries and retail locations.

Favourable access to pipeline capacity and the integrated nature of the business help Suncor get West Texas Intermediate (WTI) pricing for most of its production, as compared to the discounted Western Canadian Select (WCS) price. Nonetheless, Suncor still needs WTI to be strong to turn decent profits in the upstream division. The company's WTI breakeven price sits around US$35 per barrel.

WTI trades near US$40 per barrel right now. It was as high as $63 in January and the futures market briefly dipped below zero in April. Analysts have different views on where oil is headed in the next 12-24 months.

The bears anticipate a slow recovery in the global economy as the coronavirus continues to spread. Government lockdowns and travel restrictions could remain in place for longer than expected if the pandemic remains a serious problem through 2021. This would cap a recovery in oil demand and keep prices low.

Oil bulls say the price of oil could surge to US$100 or higher in the next two or three years. They believe that massive investment cuts across the industry will result in supply shortages as the global recovery picks up speed. A V-shaped economic rebound supported by a COVID-19 vaccine could bring oil demand back to 2019 levels, or even push higher.

Fuel demand

Suncor's refining and retail operations normally provide a decent hedge against dips in the price of oil, but the pandemic hit these operations hard. The airline industry effectively shut down in recent months and is still only operating at 10-20% of pre-pandemic capacity. Lockdowns forced employees to work from home, putting a dent in demand for gasoline.

Analysts see jet fuel demand to remaining weak for some time, as airlines say they will not be back to 2019 capacity for at least three years. Again, the widespread availability of a coronavirus vaccine is key to the recovery in international travel.

On the commuter side, gasoline demand should recover quickly. People might decide to commute to work by car rather than take public transportation as companies move staff back to the office.

Is Suncor stock a buy today?

The board cut the dividend by more than 50% to preserve cash through the downturn. The new distribution should be safe and currently offers a 3.6% yield. Suncor trades close to $23 at the time of writing. The stock fell to a closing low near $15 in March, but was as high as $45 in January.

Contrarian investors who are of the opinion that the global economy is headed for a strong recovery in 2021 might want to add Suncor to the portfolios today. The stock appears cheap under that scenario.

Oil bears who anticipate an L-shaped recovery and persistent low oil prices should look for other opportunities in the market.

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