Suncor (TSX:SU) Stock: Buy Now or Wait?

Description

Suncor Energy (TSX:SU)(NYSE:SU) and its peers continue to trade at depressed prices. This has contrarian investors wondering if energy stocks might be attractive bets right now.

Let's take a look at the current situation to see if Suncor deserves to be on your buy list.

Oil market

West Texas Intermediate (WTI) oil currently trades near US$42 per barrel. The price rebounded steadily over the past few months after the futures market briefly went negative in April.

What happened?

COVID-19 lockdowns across the globe hammered fuel demand from airlines, commuters, and commercial vehicle operators. Refineries reduced fuel production, leading to a severe drop in demand for crude oil. Producers initially kept pumping, but the market started to worry that global storage sites might reach capacity.

Investors holding futures contracts for May and June deliveries panicked, as they worried that they might be forced to take delivery of oil that would have no place to go.

Ultimately, the market sorted things out. Enough storage remained available and some savvy traders made a bundle on the rebound.

Upside opportunity

The massive investment cuts announced by global oil producers this spring could result in a supply pinch in the next few years. Oil demand remains weak, but it is improving as governments reopen their economies. Volatility is expected in the near term due to new COVID-19 waves and outbreaks. However, once vaccines and effective treatments are widely available, the global economic engine should roar back into overdrive.

Fuel demand could actually top previous levels as commuters decide to drive instead of taking public transportation.

Airlines expect the recovery in travel demand to take three or four years. It is too early to tell whether that's a cautious or optimistic outlook. Nonetheless, air travel should eventually rebound, as it did after previous crashes.

Should you buy Suncor stock now?

Suncor trades close to $21 per share at the time of writing. The stock dipped as low as $15 in March and topped $28 in June. In January, when WTI sat above US$65 per barrel, Suncor traded for more than $44 per share, so there is decent upside potential on a rebound.

Suncor cut its dividend by more than 50% to preserve cash flow during the pandemic. The new payout offers a 4% yield right now.

Suncor's WTI breakeven price sits around US$35 per barrel. Assuming oil prices continue to slowly drift higher, the stock price should rise on improved sentiment for producers. Suncor's downstream operations traditionally provide a nice hedge against volatility in the oil market. Unfortunately, that wasn't the case this time. The four large refineries and roughly 1,500 Petro-Canada service stations also saw revenue plunge in recent months.

With rebounding economic activity, the refining and retail businesses should see improved results. Suncor's current share price might not fully reflect the recovery potential.

Risks certainly remain for the energy producers. New lockdowns and an extended delay in economic growth could put additional pressure on Suncor's stock price in the coming months. The long-term outlook is also a question mark as electric vehicles become more common and governments push stimulus investments towards renewable energy solutions.

That said, Suncor appears cheap right now. Investors who buy today can pick up a decent yield and it wouldn't be a surprise to see the share price at $40 again within the next five years, especially if the oil market gets tight due to a lack of capital investment.

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