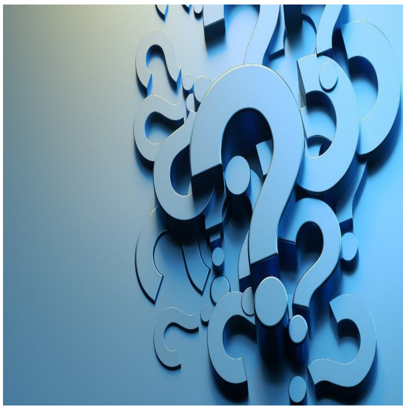

Is Suncor Stock Too Cheap to Ignore?

Description

Suncor Energy (TSX:SU)(NYSE:SU) continues to struggle amid low demand for crude oil and fuel. Investors who bought Suncor stock at the beginning of the year near $40 are not happy campers and hope for a rebound.

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Contrarian investors searching for cheap stocks wonder if Suncor might be a tempting stock pick to add to their portfolios today.

Airline industry impact on Suncor stock

Suncor is best known as a producer of crude oil at its oil sands and offshore oil facilities. At first glance, the plight of the airline industry might not be an obvious connection to Suncor's low stock price, but the two are actually strongly correlated.

Why?

Airlines consume massive amounts of fuel. In fact, jet-fuel expenses remain the highest cost for the industry. Lockdowns and travel restrictions implemented at the beginning of the pandemic forced airlines around the world to ground planes and drastically reduce flights and capacity.

Air Canada, for example, reduced capacity by 90% in Q2 compared to the same period last year. Passenger numbers fell 96% in the quarter. The Q3 results will likely show capacity down at least 80% compared to 2019 and the situation might not improve much through the end of the year.

Jet fuel is made using crude oil. Suncor is an integrated energy company, meaning it has production, refining, and retail businesses. Low oil prices hurt margins on the upstream side. Reduced fuel demand hits the refining and retail operations.

In a nutshell, the pandemic is a worst-case scenario for Suncor.

Dividend

Heading into 2020, Suncor was one of the top dividend-growth stocks on the **TSX Index** in recent years, regularly increasing the payout by double-digit percentages. In May, Suncor announced a 55% cut to the quarterly dividend, trimming the payout from $0.465 per share to $0.21.

The move is a painful shock to investors who thought the distribution would survive the downturn. The decision by the board sent a warning shot across the energy sector. If Suncor needs to protect cash flow, things must be really bad.

Suncor moved quickly to boost its liquidity and has the means to get through the crash. The new dividend payout should be safe. At the time of writing, Suncor stock provides a 5% dividend yield.

Risks

Several countries around the globe continue to struggle with rising coronavirus cases. A second wave threatens to trigger new lockdowns in parts of Europe, including France, Spain and the United Kingdom. COVID-19 cases also continue to climb throughout Latin America, Africa, and Asia.

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As a result, economic recovery could lag and that would keep a lid on demand growth for crude oil and fuel. Global airlines don’t expect to be back to 2019 capacity for at least three years.

Until a vaccine is widely available, Suncor stock remains vulnerable to shocks in the oil market.

Should you buy Suncor stock now?

Volatility should be expected in the next three to six months. However, Suncor’s share price today likely reflects most of the bad news. Contrarian investors can buy Suncor stock for less than $17. The March closing low was about $15 and the stock started 2020 around $42, so there is serious upside potential on a rebound.

Vaccines for COVID-19 should be widely available by the middle of next year. Once that occurs, travel will start to recover in step with the global economy. A surge in oil prices through the second half of 2021 is possible and this would drive Suncor stock higher.

While the coming months might be rough, Suncor appears cheap right now when you take a five-year view.

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1. Investing

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