



Replicating the Buffett Magic: Suncor Energy (TSX:SU) vs. Enbridge (TSX:ENB)

Description

Warren Buffett broke his rules this pandemic. There were many firsts for the Oracle of Omaha. For the first time, instead of buying in a market crash, he sold bank stocks and airline stocks. For the first time, he bought gold stocks and invested in a cloud initial public offering (IPO). While he changed some rules to adjust to the new post-pandemic world, he stuck to his traditional investing style and invested in energy stocks.

Buffett purchased **Dominion Energy's** natural gas pipeline business for \$10 billion in July. He increased his stake in **Suncor Energy** ([TSX:SU](#))([NYSE:SU](#)) to 1.3% by adding five million shares in June. This was the time when oil prices recovered partially from -\$30 in April to \$40/barrel in June. The prices recovered as OPEC+ asked oil companies to reduce production to balance demand and supply.

Why Buffett invested in Suncor Energy

Buffett's investment shows that [he believes the oil prices would return](#) to the pre-pandemic level of over \$60/barrel. And yes, oil prices will rise. How?

The oil giants are cutting down their capital expenditure to save money. This will tighten the oil supply when the demand returns. The demand-supply dynamics would drive the oil price. An increase in oil demand would boost Suncor Energy's retail operations of gas stations and other petroleum products. But this recovery could take almost three years as it earns a major portion of its revenue from jet fuel. Until air travel demand returns and airports are busy again, oil demand won't recover to the level where Suncor makes profits.

Hence, Suncor is walking in **Air Canada's** footsteps. The oil giant has reduced capital spending and operating costs by \$1.9 billion and \$1 billion, respectively, and increased liquidity to \$8.65 billion. It is doing everything to control its widening losses, which reached \$4.14 billion in the first half. It is even reducing its workforce by 15% in 18 months, calling it an early implementation of the "Suncor 4.0" program.

Investors buy Suncor for its dividends as the stock has nothing but declined since 2018 by 20%. After

the pandemic, the stock dropped another 60% and is now trading at 0.75 times its sales per share. But the dividend also took a hit when Suncor announced a 55% dividend cut in May. It has the liquidity to meet its current debt obligations and keep its operations functional.

Should you trust Buffett's decision?

While Suncor's facing a lot of obstacles, Buffett is still optimistic. But sadly, his optimism failed to convince retail investors to buy into Suncor. Hence the stock's Relative Strength Index (RSI) continues to stay close to the oversold category of 30. The oil prices are already volatile, and in the current volatile market, oil has become a gamble.

If you still want exposure to oil, **Enbridge** ([TSX:ENB](#))([NYSE:ENB](#)) is a better stock and is not directly impacted by oil prices. Unlike Suncor, Enbridge neither produces nor stores, or sells oil. It only transmits oil through its pipelines for a fixed price. Enbridge is affected when oil demand is low as it doesn't get to transmit that much volume.

In the second quarter, the huge dip in oil demand reduced Enbridge's revenue by 40% year-over-year (YoY). Despite this dip, its profits fell less than 3%, and its distributed cash flow surged 6%. While the company earns 55% of its revenue from oil transmission, it earns another 40% from natural gas storage and transmission. This diversification mitigates the impact of the oil crisis on the pipeline operator.

At a time when companies are cutting or suspending dividends, Enbridge has retained its 9.8% dividend increase it [announced](#) in December 2019.

Better buy: Suncor versus Enbridge

Buffett has placed its bet on both Suncor and an Enbridge-equivalent U.S stock. Suncor stock is still trading close to its March low, whereas Enbridge stock has recovered 28%. Suncor has slashed dividends while Enbridge has increased it. Enbridge is still profitable, while Suncor is grappling with billions of dollars of losses.

Suncor's dividend yield of 5.36% is lower than Enbridge's 8.4%. Moreover, you would have a higher probability of capital appreciation in Enbridge than in Suncor.

In conclusion, Enbridge is a safer way to gain exposure to the oil industry.

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