Suncor (TSX:SU) Stock Soars on Strong Earnings: How High Could it Go?

Description

Suncor (TSX:SU)(NYSE:SU) just reported strong Q1 2021 earnings. Investors with an eye for deals wonder if Suncor stock is undervalued today.

Suncor earnings rebound

Suncor's Q1 numbers came in much better than the same period last year and even outpaced analyst expectations.

The company benefitted from rising oil prices in the upstream operations, generating overall funds from operations of $2.1 billion in the quarter. Operating earnings were $746 million, or $0.49 per share compared to a loss of $0.28 per share in the same period in 2020.

Suncor used the revenue windfall to reduce total debt by $1.1 billion in the quarter, and the company took advantage of the low share price to buy back $318 million of stock, representing about 1% of the outstanding common shares.

Efficiency gains helped boost the margins. Operating costs per barrel at the oil sands facilities dropped 20% to $23.30 and by 10% at the Syncrude site.

Outlook

West Texas Intermediate (WTI) oil trades above US$65 per barrel at the time of writing. As the global economy roars back into high gear in the coming months, oil prices could shoot even higher. In fact, analysts broadly anticipate a run to US$75 before the end of the year.

Suncor expects total production to be 740,000 – 780,000 barrels of oil equivalent per day (boe/d) this year. That's up about 10% on the midpoint guidance provided in 2020.

Suncor's downstream businesses, which include refineries and retail operations, took a big hit in 2020 as a result of the drop in demand for jet fuel, gasoline, and diesel fuel. The airline industry is slowly expected to ramp up capacity through the back half of 2021. At the same time, commuters will start returning to offices. This should drive better results in these operations heading into 2022. Suncor is targeting refinery utilization of 90-96% this year.

That said, there are risks that the oil market could reverse course. OPEC+ might decide to open up the taps again to take advantage of higher prices and rising demand. Ongoing pandemic surges in India and other countries could delay the expected in the oil market by several months.

The price of WTI oil is up from US$36 last fall, so there is the potential for a large pullback on negative news.

Dividends

Suncor cut its dividend by 55% last year to preserve cash through the downturn. The board held off boosting the payout so far this year, preferring to pay down debt and repurchase shares with excess cash. While that strategy will likely remain in place through the end of 2021, investors could see the dividend start to rise again in 2022.

The current payout provides a yield of 3%.

Is Suncor a good stock to buy now?

Suncor trades near $27 per barrel. That’s up from $15 last fall, but still well below the $40 price it fetched before the pandemic. Oil prices are nearly 10% higher now than in early 2020, so Suncor’s share price might not fully reflect the upside opportunity.

The company is making good money at current oil prices, and fuel demand should rebound in the next six to 12 months. This could drive Suncor’s profitability much higher, especially if oil extends its winning streak.

If you are an oil bull, the stock looks cheap today. It wouldn’t be a surprise to see Suncor return to $40 per share by the end of 2022.

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