Oil Below $80: Is Suncor Energy Still a Bargain?

Description

Growing concerns about economic growth have pushed oil prices back down. A barrel of West Texas Intermediate (WTI) crude oil currently trades for less than US$80. That's roughly the same price it was before Russia invaded Ukraine in February.

Oil stocks like **Suncor Energy** (TSX:SU)(NYSE:SU) are closely following this trend. The stock is 30% cheaper than it was at its peak in June. Investors must now consider what comes next. Where do oil prices go from here, and what does that mean for Suncor's valuation? Here's a closer look.

What's next for oil prices?

Predicting oil prices is a fool's errand. Traders make the mistake of focusing exclusively on supply-and-demand dynamics, whereas oil prices are determined by a complex mix of geopolitics and macroeconomic trends.

Very few people predicted Russia's invasion of Ukraine earlier this year. Even fewer believed oil prices would drop to pre-war levels, despite the ongoing conflict. Some experts, such as Pierre Andurand, were convinced each barrel would trade at US$250 by now.

Put simply, even the experts can't predict this volatile market. So, ordinary investors shouldn't attempt to place targets. Instead, it may be better to anchor your assumptions on the price floor. That means figuring out the cheapest price that each barrel of oil could trade at if the war ends and we enter a deep recession this winter.

Of all the forecasts made by experts and institutions, **Citibank** had the gloomiest outlook. Earlier this year, the bank predict oil prices would drop to US$65 per barrel this year and US$45 by next year.

Whether or not oil prices drop that low is not the point. I believe investors can use this gloomy prediction as the price floor for their valuations of oil stocks.

Suncor stock valuation

Suncor stock could be undervalued, even if oil prices fall further. That's according to an analysis by industry veteran Eric Nuttall. In July, Nuttall used Citibank's pessimistic forecast to calculate the free cash flow (FCF) yield of Canadian oil stocks. Assuming a barrel of crude oil trades at US$70, he found that most oil stocks would offer an FCF yield of 19% on average!

Put simply, oil stocks would offer a tremendous return, even if the commodity dives further next year.

Suncor's FCF yield is slightly below average at 14%. However, that's still far better than most other stocks. Suncor's FCF yield is seven times greater than the 3% dividend yield of the **TSX Index**. It's also double the earnings yield of the **TSX 60 index**.

Note that Suncor's FCF yield could be much higher if Citibank's prediction is wrong and oil prices rebound above $100 later this year.

Bottom line

Oil prices are down and unpredictable. But oil stocks like Suncor could be undervalued even in the worst-case scenario. Value-oriented investors should keep an eye on this sector.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:SU (Suncor Energy Inc.)
2. TSX:SU (Suncor Energy Inc.)

PARTNER-FEEDS

1. Business Insider
2. Flipboard
3. Koyfin
4. Msn
5. Newscred
6. Quote Media
7. Sharewise
8. Smart News
9. Yahoo CA

PP NOTIFY USER

1. kduncombe
2. vraisinghani

Category

1. Energy Stocks
2. Investing

Date
2025/08/17
Date Created
2022/09/27
Author
vraisinghani