Suncor Energy Stock: Has it Bottomed Out?

Description

Suncor Energy (TSX:SU) has had a poor run in the last few weeks. On January 26, it was trading at $46. On Wednesday morning, it was at $44.29, meaning that the stock fell 3.7% from its highs. That's not the most severe stock pullback in the last 12 months — a period in which Suncor has risen. But in 2023, with oil prices trending lower than 2022 levels, it's worth exploring whether or not Suncor has bottomed out. We can start by looking at the factors that caused SU stock to fall in the first place.

Suncor Energy is very sensitive to oil prices

The main reason why Suncor Energy stock has been falling lately is because oil prices have been falling. West Texas Intermediate futures started the year at US$80 and are now at US$78. That's a 2.5% price decline. We'd expect it to impact Suncor Energy stock, because Suncor makes money by extracting, refining, and selling oil. Suncor's main business activity is selling crude oil. This business makes more money when oil rises and makes less money when oil prices fall.

Suncor's secondary business activity is operating gas stations. This business is also correlated with the price of oil. The correlation between oil and gasoline is not perfect, but it is fairly strong. Fuels Institute estimates the correlation at 0.89, which is extremely high. So, both of Suncor's main business activities are correlated with the price of oil.

In a sense, then, the answer to the question I started this article with is fairly obvious. The answer is, " No, there is no guarantee that Suncor has bottomed out." If oil goes lower, then Suncor should go lower, too — at least in the short run.

In my coverage of oil stocks last year, I frequently said that oil stocks were fairly cheap, even assuming the price of oil goes down. Suncor trades at a mere eight times earnings right now; if oil stays near US$75, then SU's P/E ratio won't go much higher than 10. So, in the long run, it may still do well, but in the short run, it absolutely could go lower, as short-term oil price fluctuations heavily influence oil stock prices. So, we need to look at the reasons why oil prices are falling.

Why oil is going down

The reason why oil is going down this year is because Russia's invasion of Ukraine hasn't disrupted the world's oil supply as much as initially feared. Russian oil is still making it to the global market: China and India are buying it in large quantities. As recently as January, European nations were still importing Russian diesel fuel.

In 2022, oil got bid up as high as $120 in the futures market, because people feared prices of $150 or higher. Today, there's not as much fear that Russian oil will disappear from the market, so people aren't hedging as much as they once were. We would not expect oil to go to $120 in this market. However, China is rapidly re-opening, and the Organization of Petroleum Exporting Countries is cutting output, so prices should stay relatively high (i.e., higher than 2021 levels).

Today's economy is no disaster for Suncor, but don't expect 2022-calibre bullishness.

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