What's Ahead for Suncor Energy Stock in 2023?

Description

Oil and gas is one of investors' favourite sectors of late, but **Suncor Energy** (TSX:SU) is not one of the loved names in the sector. Since the pandemic-led crash in 2020 — when the energy sector started its transformation story — TSX energy stocks have returned more than 350%. In the same period, Suncor Energy stock has returned 150%, notably underperforming its peers.

Suncor Energy stock compared to peers

Suncor Energy is a leading oil sands producer in Canada and produces 0.74 million barrels of oil per day. In the last 12 months, it reported total free cash flows of $9.4 billion, marking a decent 30% increase compared to 2021. Apart from financial growth, Suncor Energy's balance sheet notably strengthened due to rapid deleveraging. This has been the theme across the sector, and almost all energy companies have rapidly repaid the debt in the last few years.

Suncor Energy will report its earnings for the fourth quarter (Q4) of 2022 and full year on February 14, 2023. While the numbers are expected to come higher, how the balance sheet improved in Q4 will also be important to see. Moreover, management's guidance on how it plans to use its excess free cash flow this year will be vital for its stock.

Suncor plans to invest $5.6 billion in capital projects this year, representing a nearly 12% increase over last year. However, this higher capex is a result of higher cost inflation, and very little of it will go toward production growth.

Financial growth and share buybacks

For Q4 2022, analysts expect Suncor Energy to report total revenues of $12.7 billion, implying a 13% increase year over year. Notably, analysts expect its per-share earnings to almost double in Q4 2022 versus Q4 2021.

Suncor bought back 6.8 million shares in January 2023, marking a solid start to shareholder returns.

Along with dividends, Canadian energy companies have opted for share repurchases. Buybacks offer more flexibility to managements and help lift share prices in the short term. SU stock currently offers a decent dividend yield of 4.7%, which is in line with Canadian energy bigwigs.

However, some of the operational issues have been hindering Suncor Energy's growth for the last few quarters. Refinery outages and worker deaths at its sites have been quite concerning and have weighed on its performance. Its Commerce City refinery was shut down for six weeks and came online last week. It has a refining capacity of 98,000 barrels of oil per day. Notably, the outage could weigh on its Q1 2023 earnings.

On the valuation front, SU stock is currently trading three times its 2023 cash flows and looks discounted. TSX energy stocks, on average, are trading 3.5 times their cash flows. Moreover, SU is trading at a free cash flow yield of 16% — another valuation measure indicating a discount compared to peers.

Conclusion

Suncor Energy looks better placed to play well this year with its undervalued stock, decent financial growth, and strong balance sheet. Its decision to retain the retail distribution network should improve its contribution to its downstream business. Investors can expect a decent total return from Suncor Energy, driven by its dividends and capital appreciation and fueled by buybacks.

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