Suncor Energy Inc. (SU)

Updated February 8th, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	$42	**5 Year CAGR Estimate:**	5.8%	**Volatility Percentile:**	54.0%
Fair Value Price:	$32	**5 Year Growth Estimate:**	7.0%	**Momentum Percentile:**	56.1%
% Fair Value:	131%	**5 Year Valuation Multiple Estimate:**	-5.2%	**Growth Percentile:**	64.8%
Dividend Yield:	4.0%	**5 Year Price Target**	$45	**Valuation Percentile:**	10.7%
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Total Return Percentile:**	19.8%

Overview & Current Events

Suncor Energy is one of the largest integrated energy producers in Canada. The company is involved in all aspects of the energy value chain, including exploration & production, marketing, and refining. The company operates in three segments: Exploration & Production, Refining & Marketing, and Other. Suncor is headquartered in Calgary, Alberta, Canada and is cross-listed on both the Toronto Stock Exchange and the New York Stock Exchange, where it trades under the ticker 'SU' with a market capitalization of US$51 billion. Suncor reports financial results in Canadian dollars. Accordingly, the figures listed in this research report are in CAD and the company's TSE listed shares have been used for the purpose of valuation analysis.

In early February, Suncor reported (2/5/19) financial results for the fourth quarter of fiscal 2018. In the quarter, the company achieved record total oil sands production of 740,800 barrels per day. However, the price of oil collapsed during the quarter. Even worse, the discount of Western Canadian crude to WTI rose dramatically. Consequently, Suncor posted losses of $0.18 per share (vs. earnings of $0.84 per share in prior year's quarter). The results would have been worse if the refining segment had not benefited from reduced feedstock costs thanks to the discount of Western Canadian crude to WTI. Despite the 25% decrease in the annual earnings-per-share, management remained confident in growing production and cash flows in the upcoming years and thus raised the dividend by 17% and approved a $2 billion share repurchase program. This is sufficient to reduce the share count by approximately 3% at the current stock price.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$0.95	$1.71	$2.67	$1.79	$2.60	$1.84	-$1.38	$0.27	$2.68	$2.02	***$2.30***	***$3.23***
DPS	$0.30	$0.40	$0.43	$0.50	$0.73	$1.02	$1.14	$1.16	$1.28	$1.44	***$1.68***	***$2.08***
Shares	1559.8	1565.5	1558.6	1523.1	1478.3	1444.1	1446.0	1667.9	1641.0	1599.0	***1550.0***	***1450.0***

Although the company had a very difficult year in 2015, Suncor's recovery is well underway. Indeed, the company's 2017 earnings-per-share were its highest *in the last decade*. Moreover, Suncor expects to achieve additional growth thanks to the ramp-up of production at Fort Hills and Hebron and other growth projects. We believe that Suncor Energy is capable of generating 7% earnings-per-share growth over full economic cycles. On the other hand, the losses posted in the latest quarter are a harsh reminder of the company's sensitivity to oil prices, particularly the discount of Canadian crude to WTI. Investors should also note the markedly volatile performance record of Suncor.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	35.0	19.7	13.6	17.8	13.0	21.8	---	---	15.6	23.7	***18.3***	***14.0***
Avg. Yld.	0.9%	1.2%	1.2%	1.6%	2.2%	2.5%	3.1%	3.2%	3.1%	3.0%	***4.0%***	***4.6%***

Like many large energy companies, Suncor's valuation history has been very volatile, as the company has battled tremendous fluctuations in its earnings-per-share. Using peak earnings (which Suncor is currently approaching), we believe that a fair price-to-earnings ratio for this energy company is 14. Suncor is currently trading at a price-to-earnings

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ratio of 18.3, which is much higher than our assumed fair ratio of 14. If the stock approaches our fair valuation level over the next five years, it will incur a 5.2% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	31.6%	23.4%	16.1%	27.9%	28.1%	55.4%	N/A	43.0%	47.8%	71.3%	***73.0%***	***64.4%***

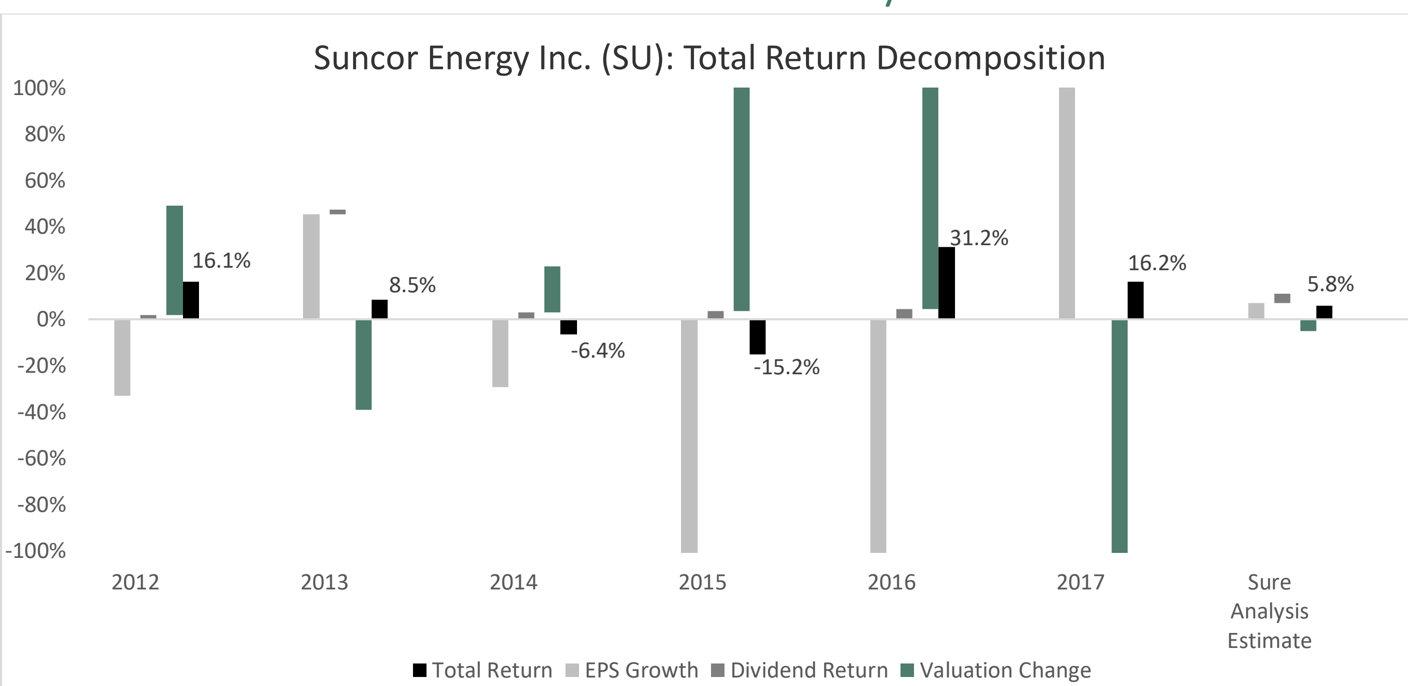
The integrated structure of Suncor Energy somewhat mitigates its exposure to the fluctuations of commodity prices. However, the company is still very sensitive to the underlying crude oil prices. In addition, as a commodity producer, Suncor lacks a meaningful competitive advantage. On the bright side, the company has a healthy balance sheet, with less than 50% of its assets financed through liabilities and high interest coverage ratio.

Suncor is a committed dividend grower. The company is a member of the S&P/TSX Canadian Dividend Aristocrats Index, which is comprised of companies included in the S&P Canada BMI that have increased their dividends for at least five consecutive years. Suncor's dividend growth streak extends well beyond this arbitrary five-year cutoff, but what really stands out is the pace of these dividend increases. Suncor has grown its dividend more than 5-fold in the last decade. However, while its 4.0% dividend yield is twice as much as the yield of the S&P, the high cyclicality of the stock and its volatile performance render its dividend unsuitable for income-oriented investors with a low level of risk tolerance.

Final Thoughts & Recommendation

Since our research report in August, in which we advised investors to sell Suncor Energy, the stock has lost 22%. As a result, the stock has become more reasonably valued but still it is likely to offer just a 5.8% average annual return over the next five years. Therefore, due to its volatile performance record and its full valuation right now, Suncor Energy earns a hold recommendation from Sure Dividend at current prices. Of course this volatile stock may offer large gains if the oil price enjoys a strong rebound but we prefer other stocks in the energy sector, with a less volatile record and lower exposure to deeply discounted Canadian crude oil.

Total Return Breakdown by Year



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Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	25998	32604	38339	38107	39593	39862	29208	26807	32051	38542
Gross Profit	9683	17070	16662	14614	17408	16194	10118	10813	15329	18671
Gross Margin	37.2%	52.4%	43.5%	38.3%	44.0%	40.6%	34.6%	40.3%	47.8%	48.4%
SG&A Exp.	6430	7984	2723	3475	2861	3507	3428	4047	3734	10453
Operating Profit	1048	5065	7262	4622	7048	5292	68	142	4678	6675
Op. Margin	4.0%	15.5%	18.9%	12.1%	17.8%	13.3%	0.2%	0.5%	14.6%	17.3%
Net Profit	1146	3829	4304	2740	3911	2699	-1995	434	4458	3293
Net Margin	4.4%	11.7%	11.2%	7.2%	9.9%	6.8%	-6.8%	1.6%	13.9%	8.5%
Free Cash Flow	-1445	-524	3138	1902	3323	1975	217	-902	2415	5174
Income Tax	213	1947	2765	2244	2465	1891	-32	-359	1458	1690

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	69746	68607	74741	76401	78315	79671	77527	88702	89494	89579
Cash & Equivalents	505	1077	3781	4385	5202	5495	4049	3016	2672	2221
Acc. Receivable	3703	5253	5383	5201	5254	4275	2751	3182	3281	3206
Inventories	2947	3141	4169	3697	3944	3466	3090	3240	3468	3159
Goodwill & Int.	3201	3422	3114	3104	3092	3083	3079	3075	3061	3061
Total Liabilities	35635	33415	36149	37186	37135	38068	38488	44072	44111	45574
Accounts Payable	6307	6443	7742	6446	7090	5704	5306	5588	6203	5647
Long-Term Debt	13882	12331	10777	11024	11458	13329	15303	17430	15579	17350
Total Equity	34111	35192	38592	39215	41180	41603	39039	44630	45383	44005
D/E Ratio	0.41	0.35	0.28	0.28	0.28	0.32	0.39	0.39	0.34	0.39

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	2.2%	5.5%	6.0%	3.6%	5.1%	3.4%	-2.5%	0.5%	5.0%	3.7%
Return on Equity	4.7%	11.1%	11.7%	7.0%	9.7%	6.5%	-4.9%	1.0%	9.9%	7.4%
ROIC	3.3%	8.0%	8.9%	5.5%	7.6%	5.0%	-3.7%	0.7%	7.2%	5.4%
Shares Out.	1559.8	1565.5	1558.6	1523.1	1478.3	1444.1	1446.0	1667.9	1641.0	1599.0
Revenue/Share	21.47	20.69	24.23	24.60	26.36	27.21	20.19	16.63	19.25	23.66
FCF/Share	-1.19	-0.33	1.98	1.23	2.21	1.35	0.15	-0.56	1.45	3.18

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.