Suncor Energy Inc. (SU)

Updated May 21st, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	$18	**5 Year CAGR Estimate:**	12.4%	**Market Cap:**	$26.3 B
Fair Value Price:	$20	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	6/3/2020
% Fair Value:	92%	**5 Year Valuation Multiple Estimate:**	1.6%	**Dividend Payment Date:**	6/25/2020
Dividend Yield:	3.3%[1]	**5 Year Price Target**	$29	**Years Of Dividend Growth:**	0
Dividend Risk Score:	F	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	N/A

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$26.3 billion. Suncor reports financial results in Canadian dollars. However, the figures listed in this research report are in USD.

In early May, Suncor reported (5/5/20) financial results for the first quarter of fiscal 2020. Total upstream production fell -3.2% over last year's quarter. Even worse, the company was hurt by the collapse of the oil price, which was caused by the spread of the coronavirus and the resultant plunge in the demand for oil. As a result, Suncor switched from an adjusted profit of $0.59 per share in last year's quarter to an adjusted loss of -$0.15 per share. Due to the severe downturn in the energy market, Suncor cut its dividend by -55% and thus broke its 18-year dividend growth streak (in CAD). Due to suppressed oil prices and weak demand for refined products, we expect the company to lose -$1.50 per share this year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$1.66	$2.70	$1.79	$2.52	$1.60	-$1.04	$0.20	$2.06	$1.56	$2.18	***-$1.50***	***$2.20***
DPS	$0.39	$0.43	$0.50	$0.71	$0.89	$0.86	$0.84	$0.99	$1.11	$1.27	***$0.60***	***$0.80***
Shares[2]	1,566	1,559	1,523	1,478	1,444	1,446	1,668	1,641	1,585	1,536	***1,529***	***1,480***

Suncor will be greatly affected by the pandemic this year, but we expect the company to begin to recover next year, along with the energy market. Suncor expects to achieve growth thanks to the ramp-up of production at Fort Hills and Hebron and other growth projects, which enhance value within its integrated asset portfolio. The company also makes sustained efforts to reduce its operating expenses. Overall, we expect Suncor to grow its earnings-per-share by 8.0% per year on average off its mid-cycle (4-year average) earnings-per-share of $1.50. Despite the strong results in recent years, the losses posted in the last quarter of 2018 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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	19.7	13.6	17.8	13.0	21.8	---	---	15.6	23.7	14.4	***12.0***	***13.0***
Avg. Yld.	1.2%	1.2%	1.6%	2.2%	2.5%	3.1%	3.2%	3.1%	3.0%	4.0%	***3.3%***	***2.8%***

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. As we expect the company to recover over the next five years, we

[1] Forward dividend yield.
[2] In millions.
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.

believe that a fair price-to-earnings ratio for this energy company in 2025 is 13. Suncor is currently trading at a price-to-earnings ratio of 12.0, which is lower than our assumed fair ratio of 13. If the stock approaches our fair valuation level over the next five years, it will enjoy a 1.6% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	23.4%	16.1%	27.9%	28.1%	55.4%	---	43.0%	47.8%	71.3%	58.0%	***40.0%***	***36.4%***

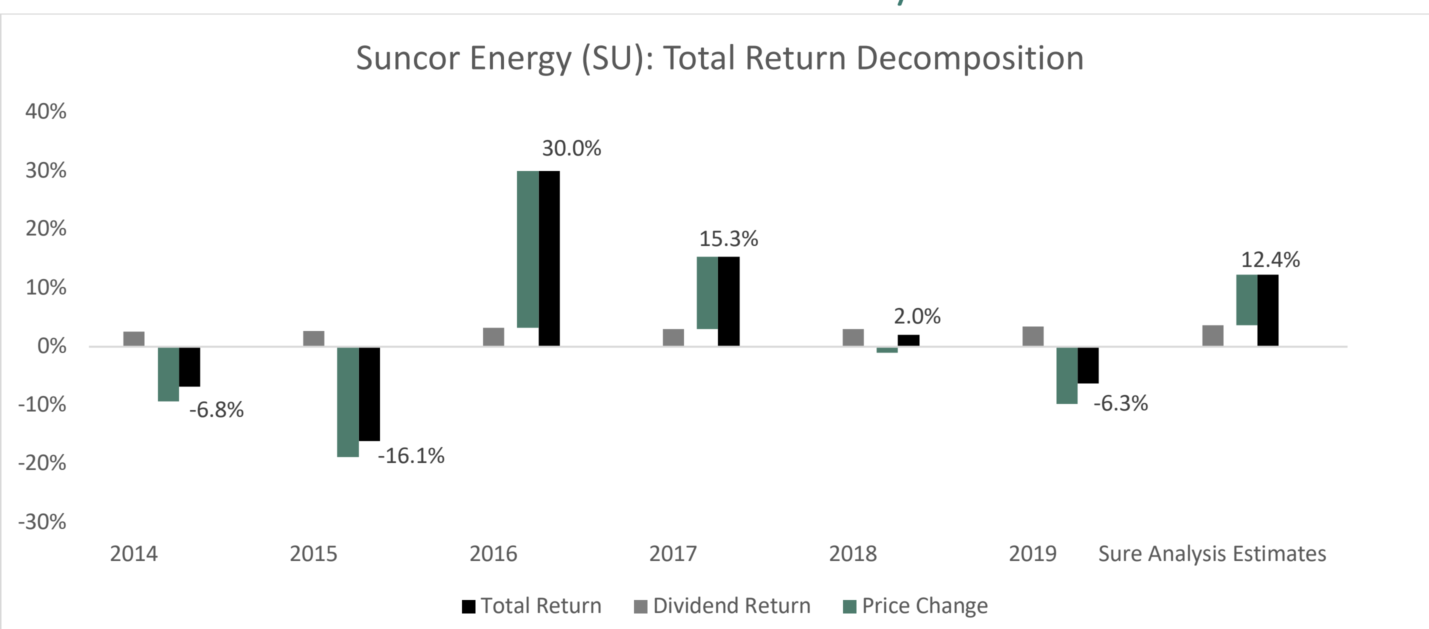
The integrated structure of Suncor Energy somewhat mitigates its exposure to the fluctuations of commodity prices. However, the company is still very sensitive to underlying crude oil prices. In addition, as a commodity producer, Suncor lacks a meaningful competitive advantage. On the bright side, the company has a decent balance sheet, with only 54% of its assets financed through liabilities and a healthy interest coverage ratio.

Until recently, Suncor was 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 extended well beyond this arbitrary five-year cutoff, but its high sensitivity to oil prices and its vulnerability to downturns forced the company to end its 18-year dividend growth streak (in CAD) in the ongoing downturn. The high cyclicality of the stock and its volatile performance render its dividend unsuitable for income-oriented investors.

Final Thoughts & Recommendation

Due to the impact of the coronavirus on the demand for oil products, Suncor Energy has lost half of its market cap in about four months. We expect the pandemic to subside and the energy market to recover from next year. As a result, Suncor could offer a 12.4% average annual return over the next five years and thus earns a buy rating. Nevertheless, due to its volatile performance record and its high sensitivity to oil prices, the stock will be vulnerable if the ongoing downturn lasts longer than anticipated. Therefore, the stock is suitable only for patient investors, who can endure stock price pressure for a considerable period.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	31,611	38,773	38,118	38,450	36,107	22,884	20,243	24,656	29,741	28,890
Gross Profit	16,550	16,851	14,618	16,905	14,668	7,927	8,165	11,753	14,408	11,460
Gross Margin	52.4%	43.5%	38.3%	44.0%	40.6%	34.6%	40.3%	47.7%	48.4%	39.7%
SG&A Exp.	7,741	2,754	3,503	3,111	3,196	2,781	3,087	2,940	3,211	3,666
Operating Profit	4,911	7,344	4,596	6,512	4,774	(42)	76	3,551	4,959	1,483
Op. Margin	15.5%	18.9%	12.1%	16.9%	13.2%	-0.2%	0.4%	14.4%	16.7%	5.1%
Net Profit	3,712	4,353	2,741	3,798	2,445	(1,563)	328	3,440	2,541	2,184
Net Margin	11.7%	11.2%	7.2%	9.9%	6.8%	-6.8%	1.6%	14.0%	8.5%	7.6%
Free Cash Flow	(508)	3,174	1,903	3,227	1,789	170	(681)	1,863	3,993	3,664
Income Tax	1,888	2,796	2,245	2,394	1,713	(25)	(271)	1,125	1,304	(276)

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	68,596	73,211	76,798	73,551	68,631	55,868	65,790	71,168	65,769	68,466
Cash & Equivalents	1,077	3,704	4,408	4,886	4,734	2,918	2,237	2,125	1,631	1,500
Acc. Receivable	5,252	5,273	5,228	4,934	3,683	1,982	2,360	2,609	2,354	3,102
Inventories	3,140	4,084	3,716	3,704	2,986	2,227	2,403	2,758	2,319	2,879
Goodwill & Int.	3,421	3,050	3,120	2,904	2,656	2,219	2,281	2,434	2,247	2,341
Total Liabilities	33,410	35,409	37,379	34,876	32,793	27,735	32,688	35,078	33,460	36,281
Accounts Payable	6,442	7,584	6,480	6,659	4,914	3,824	4,145	4,933	4,146	5,018
Long-Term Debt	12,329	10,556	11,081	9,771	10,592	10,114	12,928	11,396	12,738	11,513
Total Equity	35,186	37,802	39,419	38,675	35,838	28,132	33,102	36,090	32,308	32,185
D/E Ratio	0.35	0.28	0.28	0.25	0.30	0.36	0.39	0.32	0.39	0.36

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	5.5%	6.1%	3.7%	5.1%	3.4%	-2.5%	0.5%	5.0%	3.7%	3.3%
Return on Equity	11.0%	11.9%	7.1%	9.7%	6.6%	-4.9%	1.1%	9.9%	7.4%	6.8%
ROIC	8.0%	9.1%	5.5%	7.7%	5.2%	-3.7%	0.8%	7.4%	5.5%	4.9%
Shares Out.	1,566	1,559	1,523	1,478	1,444	1,446	1,668	1,641	1,585	1,536
Revenue/Share	20.06	24.51	24.61	25.60	24.65	15.82	12.56	14.81	18.26	18.51
FCF/Share	(0.32)	2.01	1.23	2.15	1.22	0.12	(0.42)	1.12	2.45	2.35

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