Suncor Energy Inc. (SU)

Updated February 17th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	$19	**5 Year CAGR Estimate:**	11.4%	**Market Cap:**	$29.0 B
Fair Value Price:	$20	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	3/3/2021
% Fair Value:	97%	**5 Year Valuation Multiple Estimate:**	0.5%	**Dividend Payment Date:**	3/25/2021
Dividend Yield:	3.5%	**5 Year Price Target**	$29	**Years Of Dividend Growth:**	0
Dividend Risk Score:	F	**Retirement Suitability Score:**	F	**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 the 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$29.0 billion. Suncor reports financial results in Canadian dollars. However, the figures listed in this research report are in USD.

In early February, Suncor reported (2/3/21) financial results for the fourth quarter of fiscal 2020. Total upstream production decreased -1% over the prior year's quarter while the pandemic caused a greater than -25% plunge in the average realized price of oil and refining margin of Suncor. As a result, the company switched from an adjusted profit of $0.40 per share to an adjusted loss of -$0.07 per share. Due to the severe downturn in the energy market, Suncor cut its quarterly dividend by -55% last year and thus it broke its 18-year dividend growth streak (in CAD). On the bright side, the pandemic could subside in the second half of this year while the price of oil has rallied to pre-COVID levels thanks to the aggressive production cuts of OPEC and Russia. As a result, Suncor is poised to recover strongly.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$2.70	$1.79	$2.52	$1.60	-$1.04	$0.20	$2.06	$1.56	$2.18	-$1.15	***$0.80***	***$2.20***
DPS	$0.43	$0.50	$0.71	$0.89	$0.86	$0.84	$0.99	$1.11	$1.27	$0.83	***$0.66***	***$0.88***
Shares[1]	1,559	1,523	1,478	1,444	1,446	1,668	1,641	1,585	1,536	1,525	***1,525***	***1,480***

Suncor was greatly affected by the pandemic last year, but we expect the company to begin to recover this 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 2017-2019, 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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	13.6	17.8	13.0	21.8	---	---	15.6	23.7	14.4	---	***12.7***	***13.0***
Avg. Yld.	1.2%	1.6%	2.2%	2.5%	3.1%	3.2%	3.1%	3.0%	4.0%	4.6%	***3.5%***	***3.1%***

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 believe that a fair price-to-earnings ratio for this energy company in 2026 is 13. Suncor is currently trading at a price-to-

[1] 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.

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earnings ratio of 12.7, which is slightly lower than our assumed fair ratio of 13.0. If the stock trades at our fair valuation level in five years, it will enjoy a modest 0.5% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	16.1%	27.9%	28.1%	55.4%	---	43.0%	47.8%	71.3%	58.0%	---	***44.0%***	***40.1%***

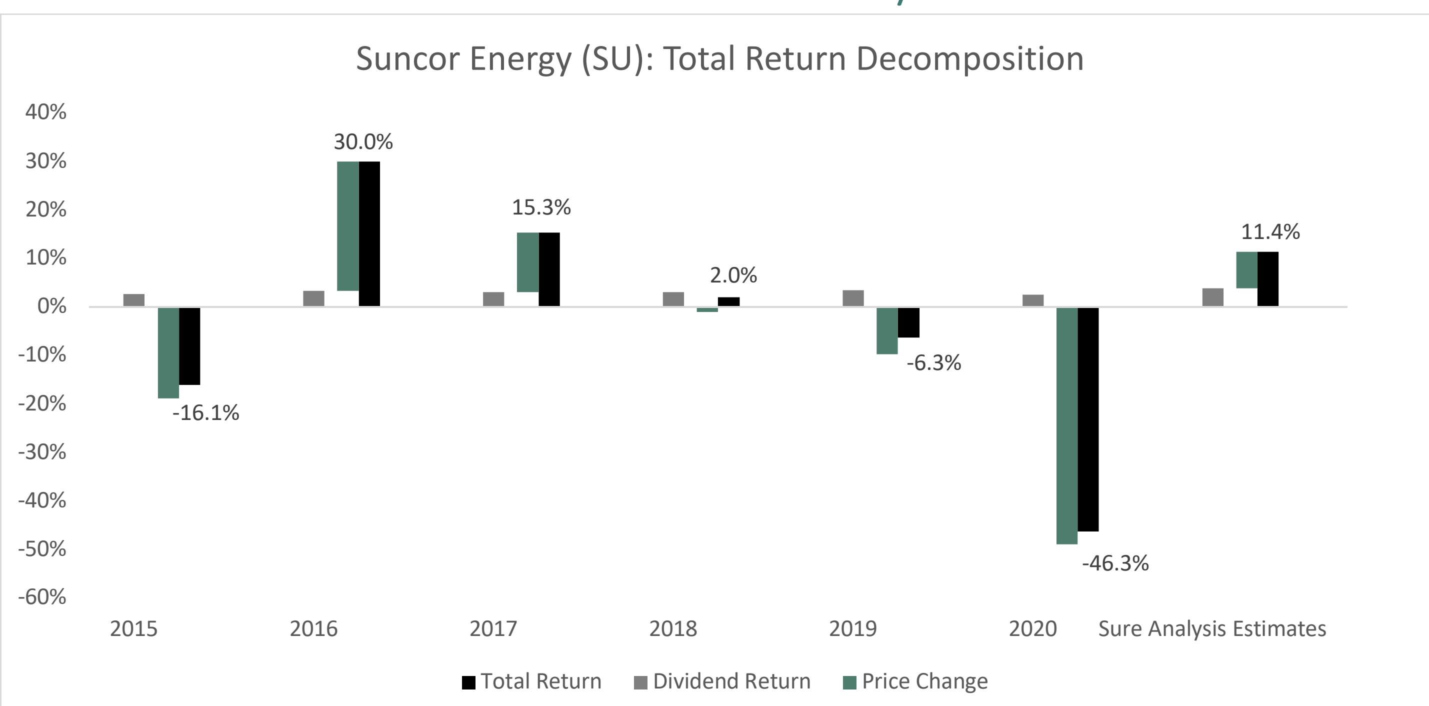
The integrated structure of Suncor Energy somewhat mitigates its exposure to the fluctuations of commodity prices. However, the company is still very sensitive to the underlying crude oil prices. In addition, as a commodity producer, Suncor lacks a meaningful competitive advantage. On the bright side, the company has a decent balance sheet, with only 58% 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

We expect the pandemic to subside and the energy market to recover later this year. Suncor has rallied 65% off its bottom in November but it still has strong upside potential. We expect Suncor to offer an 11.4% average annual return over the next five years and thus we maintain our buy rating. Nevertheless, due to its volatile performance record and its high sensitivity to oil prices, the stock will be vulnerable if the pandemic lasts longer than expected. 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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	38,773	38,118	38,450	36,107	22,884	20,243	24,656	29,741	28,890	18,407
Gross Profit	16,851	14,618	16,905	14,668	7,927	8,165	11,753	14,408	11,460	4,496
Gross Margin	43.5%	38.3%	44.0%	40.6%	34.6%	40.3%	47.7%	48.4%	39.7%	24.4%
SG&A Exp.	2,754	3,503	3,111	3,196	2,781	3,087	2,940	3,211	3,666	7,409
Operating Profit	7,344	4,596	6,512	4,774	(42)	76	3,551	4,959	1,483	(4,205)
Op. Margin	18.9%	12.1%	16.9%	13.2%	-0.2%	0.4%	14.4%	16.7%	5.1%	-22.8%
Net Profit	4,353	2,741	3,798	2,445	(1,563)	328	3,440	2,541	2,184	(3,224)
Net Margin	11.2%	7.2%	9.9%	6.8%	-6.8%	1.6%	14.0%	8.5%	7.6%	-17.5%
Free Cash Flow	3,174	1,903	3,227	1,789	170	(681)	1,863	3,993	3,664	(934)
Income Tax	2,796	2,245	2,394	1,713	(25)	(271)	1,125	1,304	(276)	(1,327)

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	73,211	76,798	73,551	68,631	55,868	65,790	71,168	65,769	68,466	66,357
Cash & Equivalents	3,704	4,408	4,886	4,734	2,918	2,237	2,125	1,631	1,500	1,478
Acc. Receivable	5,273	5,228	4,934	3,683	1,982	2,360	2,609	2,354	3,102	2,476
Inventories	4,084	3,716	3,704	2,986	2,227	2,403	2,758	2,319	2,879	2,837
Goodwill & Int.	3,050	3,120	2,904	2,656	2,219	2,281	2,434	2,247	2,341	2,610
Total Liabilities	35,409	37,379	34,876	32,793	27,735	32,688	35,078	33,460	36,281	38,316
Accounts Payable	7,584	6,480	6,659	4,914	3,824	4,145	4,933	4,146	5,018	3,673
Long-Term Debt	10,556	11,081	9,771	10,592	10,114	12,928	11,396	12,738	11,513	14,736
Total Equity	37,802	39,419	38,675	35,838	28,132	33,102	36,090	32,308	32,185	28,041
D/E Ratio	0.28	0.28	0.25	0.30	0.36	0.39	0.32	0.39	0.36	0.53

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	6.1%	3.7%	5.1%	3.4%	-2.5%	0.5%	5.0%	3.7%	3.3%	-4.8%
Return on Equity	11.9%	7.1%	9.7%	6.6%	-4.9%	1.1%	9.9%	7.4%	6.8%	-10.7%
ROIC	9.1%	5.5%	7.7%	5.2%	-3.7%	0.8%	7.4%	5.5%	4.9%	-7.5%
Shares Out.	1,559	1,523	1,478	1,444	1,446	1,668	1,641	1,585	1,536	1,525
Revenue/Share	24.51	24.61	25.60	24.65	15.82	12.56	14.81	18.26	18.51	12.06
FCF/Share	2.01	1.23	2.15	1.22	0.12	(0.42)	1.12	2.45	2.35	(0.61)

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