

# PALOS

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## Weekly Commentary

Issue No. 19 | MAY 10, 2021

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## Suncor Energy Inc. – The Future Looks Bright

**Suncor Energy Inc.** (TSX, NYSE: SU) is Canada's largest integrated energy company with operations focused on the Athabasca oil sands. The company uses upgrading technologies to extract and convert oil bitumen into feedstocks that supply refineries. Other operations include natural gas, petrochemicals and a nationwide retail gasoline network that operates under the Petro-Canada banner. Suncor also has a presence in Libya, Norway, Syria, and the United Kingdom.

Suncor reported first-quarter results on May 3. Funds from operations generated C\$2.1 billion, "far exceeding all capital expenditures and dividend commitments" according to CEO Mark Little. The strong performance has allowed SU to comfortably proceed with plans to significantly reduce debt and meet stock buyback targets of roughly 1% of outstanding shares. Total debt was reduced by approximately C\$1.1 billion. Cash flow was C\$2.35 billion (C\$1.54/share) compared to C\$1.38 billion (C\$1.54/share) in the first quarter of 2020. Earnings per share (EPS) of 54 cents far exceed the comparable Q1/2020 net loss of C\$3.5 billion (\$2.31 per share).

Over the last two quarters, Suncor realized record Synthetic Crude Oil (SCO) production. In Q1/2021 oil sands cash operating costs per barrel decreased by approximately 20% while Syncrude costs fell by roughly 10%. The Syncrude project, which is a joint venture between Suncor (59%), Imperial Oil (25%), Sinopec (9%), and CNOC (7%), is one of the largest oil sands projects in the world. Suncor will assume 100% of Syncrude's operational responsibilities by the final quarter of 2021. It is expected that the transition will create significant synergies and cost efficiencies. The integration will elevate competitiveness from a global perspective.

In recent years, Canada's oil sands have attracted more than their share of negative publicity from climate change interest groups, politicians, institutional investors, and even celebrities. The pressure to reduce GHG (Green House Gas) emissions has become a critical issue facing the oil and gas industry. While weening off oil in the short-term is practically impossible, initiatives are being undertaken to reduce the environmental impact and improve sustainability. Suncor has taken significant strides towards the development of new technologies designed to reduce GHG, increase energy efficiency at all facilities and participate in renewable energy initiatives like wind and carbon capture.

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Despite the challenges posed by the pandemic (e.g., plummeting crude prices, demand destruction, operational) we have seen a remarkable recovery in the energy sector. Over the last several quarters, Canadian exploration and production companies have been diligent in improving balance sheets by mandating cost reductions, cutting capital expenditures and improving operational efficiencies. In astounding fashion, Canada's oil patch has weathered the storm and we are optimistic on the sector. As we exit the pandemic the demand side of the equation is sure to see a resurgence.

As a prudent measure, the quarterly dividend was effectively halved in May of last year. Prior to this measure, SU has paid a reliable long-term dividend and the current yield sits at 2.9%. The balance sheet is improving and given Suncor's progressive ESG agenda we are optimistic on SU shares. The **Palos Income Fund LP** and the **Palos Equity Income Fund** currently hold shares in Suncor. The company has a market cap of C\$43 billion making it the most senior of Canada's energy production companies.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) <sup>1</sup>	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$9.75	13.83%
Palos Equity Income Fund - RRSP	PAL101	\$7.25	13.95%
Palos Merchant Fund L.P. (Dec 31, 2020) <sup>2</sup>	PAL500	\$1.35	-21.15%
Palos WP Growth Fund - RRSP	PAL210	\$23.87	49.52%
Palos-Mitchell Alpha Fund <sup>3</sup>	PAL300	\$11.91	13.07%
S&P TSX Composite (Total Return with dividends reinvested)			12.75%
S&P 500 (Total Return with dividends reinvested)			13.25%
S&P TSX Venture (Total Return with dividends reinvested)			9.14%
Chart 2: Market Data <sup>1</sup>			Value
US Government 10-Year			1.58%
Canadian Government 10-Year			1.50%
Crude Oil Spot			US \$64.90
Gold Spot			US \$1831.30
US Gov't10-Year/Moody BAA Corp. Spread			197 bps
USD/CAD Exchange Rate Spot			US \$0.8243

<sup>1</sup> Period ending May 7, 2021. Data extracted from Bloomberg

<sup>2</sup> Fund is priced annually

<sup>3</sup> Fund is priced weekly on Tuesdays

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