Suncor Energy First Quarter 2021 Financial Results Call

Tuesday, 4 May 2021

Operator: Good day and thank you for standing by and welcome to the Suncor Energy First Quarter 2021 Financial Results Conference Call. At this time all participants are in a listen-only mode. After the speakers' presentation, there will be a question and answer session. (Operator Instructions). I would now like to hand the conference over to your speaker today, Mr. Trevor Bell, VP Investor Relations. Please go ahead.

Introduction

Trevor Bell

Vice President of Investor Relations, Suncor Energy Inc.

Thank you, operator, and good morning. Welcome to Suncor's first quarter earnings call. With me this morning are Mark Little, president and chief executive officer; and Alister Cowan, chief financial officer. Please note that today's comments contain forward-looking information. The actual results may differ materially from the expected results because of various risk factors and assumptions and they are described in our first quarter earnings release as well as our current Annual Information Form. Both of these are available on SEDAR, EDGAR and our website, suncor.com.

Certain financial measures referred to in these comments are not prescribed by Canadian GAAP. For a description of these financial measures, please see our first quarter earnings release. Following formal remarks, we'll open the call up to questions.

Now, I'll hand it over to Mark for his comments.

Opening Remarks

Mark Little

President & Chief Executive Officer, Suncor Energy Inc.

Great, thanks Trevor and good morning - thank you for joining us.

Before I get into our opening remarks, I would like to note that we'll be hosting investors and the analysts' community at our virtual investor day on May 26th. On that day we'll address, in detail, the outlook for our business from an operating, and capital allocation, and ESG performance perspective. As a result, our remarks today will be focused primarily on our first quarter results.

In the first quarter we executed upon the commitments we have made to our shareholders – namely operational excellence, financial resilience, shareholder returns and fortifying our business model.

Our focus on operational excellence was reflected through combined upgrader utilization of 97%, record In Situ production of 252,000 bbls/d, and a disciplined focus on costs across the company. This performance was supported by increased upgrading flexibility achieved through Syncrude and Base Plant interconnecting pipelines. Within our Downstream business, we generated nearly $1 billion of funds flow from operations as our 92% utilization at our refineries continued their industry leadership position. Our physically integrated model generated $2.2 billion of funds from operations, excluding the restructuring charge of approximately $125 million after-tax related to our previously announced headcount reductions. We reduced our total debt by $1.1 billion and returned approximately $640 million to shareholders through dividends and share buybacks, or roughly 30% of funds from operations. Our buyback resumed at the beginning of February and including purchases made in April, we've bought back approximately 20 million shares for $530 million representing a buyback yield of 5% on our market cap on an annualized basis.

Focusing on operating performance,

Our fourth quarter call, I mentioned that the combined Base Plant and Syncrude upgraders set the second-best quarterly SCO production in our history with 514,000 bbls/d. This trend continued into the first quarter with even stronger production of 520,000 bbls/d. Together, these two quarters mark the highest ever SCO production at our combined upgrading facilities over a six-month period. This performance reflects our strategy to maximize the value of each barrel.

We have a similar good news story on costs which we continue to drive down. Many of you had recognized the improved cost performance in Q4, closing out the year at the bottom end of our 2020 guidance range. The first quarter trended 12% below these levels, reflecting the significant strides made in 2020 on the initiatives to structurally improve the cost of our business. As a result, the first quarter Oil Sands operations costs averaged $23/bbl Canadian, more than absorbing the 20% quarter-over-quarter natural gas price increase.

Syncrude achieved 94% utilization with cash operating costs of $32/bbl during the first quarter. Along with the other owners and personnel at Syncrude we are making good progress on the smooth transfer of operatorship of Syncrude to us by the end of the third quarter.

At Fort Hills, our net production averaged 51,000 bbls/d reflecting a change in the mine ramp up strategy. With full partner support, a decision was made to reset the mine plan. Over the next 4 months, we will increase the available ore inventory to provide a consistent feed to the plant while keeping our production flat. Appropriate ore inventory levels are required to operate the plant at 90% of nameplate capacity on a two-train operation. This change does not impact our production guidance range for the year – it merely changes the production profile throughout the year.

Our Downstream had another good market leading quarter, generating nearly $1 billion of funds from operation. Despite continued stay at home orders across Canada, we leveraged our midstream assets and expertise to capture robust margins, and exported significantly higher volumes. I'm confident that as you see the cracks improve and the Canadian economy unlocks as vaccinations pick up, we will continue to build on this level of profitability, both in volumes and margin increases.

Finally, and most importantly - we hold the health and safety of our employees and contractors above all else. Currently, the third wave of the pandemic in Canada is significantly impacting the region of Fort McMurray. Given this situation, and with Syncrude in the middle of turnaround schedule, we've delayed the start of our U2 turnaround at Base Plant until at least June, we will see when this gets finalized. This decision supports the completion of Syncrude turnaround and minimizes the overlap between the two assets. These measures have been taken to ensure our planned maintenance can be performed safely and efficiently. We currently expect no material impact to our 2021 guidance. We also continue to work with the community of Fort McMurray, and with governments and other industry players to accelerate rapid testing and now vaccinations in the region. We will continue to provide assistance to the community and its citizens during these trying times.

I'll now hand it over to Alister to go through our financial highlights.

Financial Highlights

Alister Cowan

Chief Financial Officer, Suncor Energy Inc.

Thanks, Mark.

In the first quarter, as Mark highlighted, Suncor generated $2.2 billion of funds from operations. Now this, as Mark said, excluded approximately $125 million of after-tax restructuring charges resulting from staffing reductions that we announced on our 2020 third quarter call. We do expect to record another restructuring charge later this year in the third quarter as we progress our Syncrude operatorship integration and as we deploy other company wide processes and technology investments across the company.

Consistent with the plans we outlined for 2021, we allocated approximately two-thirds of our free funds flow to debt repayment and one-third to share buybacks:

- We strengthened the balance sheet by reducing our total debt balance by approximately $1.1 billion. We also termed out a portion of a short-term commercial paper by issuing 30-year debt in the US and Canadian markets for an equivalent $1.5 billion Canadian – at a very appealing, 3.8% average rate. I believe this issuance demonstrates the market's confidence in the long-term viability of the oilsands and our physically integrated model.

- Restarting our share buyback program at the beginning of February, we repurchased approximately 12 million shares at $26 per share. In April we purchased an additional 8.2 million shares for $215 million. So, year to date, that's $530 million of stock repurchases for just over 20 million shares.

Our strong operational results supported our significant financial progress made in the quarter. Oilsands operations generated $1.4 billion of funds flow– nearly double Q4 levels with price realizations improving approximately 35% quarter over quarter. SCO and bitumen realizations were nearly $70/bbl Canadian and $48/bbl Canadian, respectively.

As Mark noted, we continue to progress our cost improvement performance. If I compare our aggregate Oil Sands operating, selling and general costs to Q1 2020 for seasonality, not only are the per unit costs coming down but also our absolute costs are down by nearly $300 million. This was achieved while increasing production by 60,000 bbl/d and absorbing a 50% increase in natural gas prices.

The E&P segment generated $285 million of funds from operations with price realizations of nearly $75/bbl Canadian. As you will see from our financial statements, our sales are lower than production in E&P. This is purely a timing issue. Loadings and thus sales were delayed in the quarter given some challenging sea states. We expect this to reverse, which will provide an uplift to funds from operations in the second quarter.

And finally, our Downstream recorded approximately $1 billion of funds from operations. So, this is a healthy improvement from 2020 levels despite the continued and extended stay at home orders across much of Canada. I do recognize we benefitted from a FIFO tailwind, but our industry leading utilization rates are a reflection of our integrated model, our midstream capabilities and our logistics network. Our model allows us to place volumes with the end consumer that others simply are not able to do.

As I said in February, given the current macro pricing environment and our solid operating performance, any additional free funds flow is expected to be allocated to debt repayment and share buybacks. Our capital guidance for 2021 will not change. And, we maintain our free funds flow allocation of approximately two thirds to debt repayment and one third to share buyback for 2021.

With that, I'll pass it back to Mark for some closing comments.

Mark Little
President & Chief Executive Officer, Suncor Energy Inc.

Great, Thanks, Alister.

Our first quarter results demonstrate a sharp focus towards operational excellence, financial resilience, shareholder returns and further fortifying our unique physically integrated model.

As we build on our operational momentum and as consumer demand steadily improves, particularly in Canada, we are positioned to benefit from the large tailwinds expected in 2021 to both our upstream and downstream business and our financial performance. Combined with our focus on cost, margin enhancement and capital discipline in the form of our $2 billion improvement target – the free funds flow generation capability of our business is stronger than ever.

I do hope everyone can join us on our Investor Day on May 26th. We're looking forward to sharing more details about the plans including: the initiatives that are structurally lowering our cost and our capital base; increasing the funds flow generation capabilities of our business; and adding financial resilience while targeting increased shareholder returns; and achieving all this with better environmental performance.

With that, Trevor, back to you.

Trevor Bell: Thank you, Mark and Alister. I'll turn the call back to the operator to take some questions. Operator?

Q&A

Operator: (Operator instructions). And your first question comes from the line of Greg Pardy with RBC Capital.

Greg Pardy (RBC Capital): Hey, good morning. Really just one question for me, Mark, and it's -- I guess it's digging a little bit back into Fort Hills. So, what I'm wondering is whether you've moved from, on a sustained basis from a sort of a just-in-time inventory methodology, right, in terms of ore versus a sustained buffer. And then kind of the follow-up is with the plan that you have laid out, what does that mean for exit rates and then ultimately, costs?

Mark Little: Ya. Thanks, Greg. Ya, it's an interesting way you characterize that. I guess that's a fair way of talking about it. Part of the issue with it is when you slowly ramp up, we literally are constantly changing the operation of the two-trains and in some cases, running trains for periods of time, shutting them down to average below a two-train minimum.

So, our view was, look, this is creating an enormous amount of variability within the plant. Let's just clear off the overburden, get the mine ready to go at full rates. And then in mid-Q3 or in September, we're expecting to be at full rates and be within 90% of plant capacity at year-end. And we're expecting that as you get into 2022, although we don't have all of our cost reductions implemented, but we expect to be very much in the range that we initially stated for Fort Hills, which is in the $20-$23 a barrel as you get into 2022.

Greg Pardy: Okay. Terrific. And then the last piece of that -- that's helpful. The last piece of that is just on the autonomous haul trucks, I think you've deployed all of them. How's that working? And are you seeing cost savings flipping into that as -- when it smooth?

Mark Little: Yes. As we stated before, Greg, we structurally were driving down the costs at Fort Hills. Part of that is autonomous haul trucks, but there's also lots of changes around staffing and support of the operation and such. So yes, they're up and operating, they're going well, and they're delivering on cost reductions.

Greg Pardy: Ok, terrific, thanks very much.

Mark Little: Thanks Greg.

Operator: And your next question comes from the line of Neil Mehta with Goldman Sachs.

Neil Mehta (Goldman Sachs): Ya, thank you. So, the first set of questions just around capital returns, good deleveraging in the first quarter. It looks like you picked up the pace of buybacks here in April. So just can you talk about how you're thinking about approaching the buyback in 2021? And are you pulling forward some of the share repurchase relative to your plans?

Alister Cowan: Ya, Neil, we -- in April, it was pretty consistent with the numbers that we were buying back in March. I would say that as we're generating and realizing free cash flow, we're deploying it in the 2/3 to 1/3 that we said. So, it's pretty consistent. With that, I wouldn't say we're currently pulling anything forward. As we generate the cash flow, we'll allocate it to debt repayment and buybacks and the allocations that we said.

Neil Mehta: And then the follow-up is just around the COVID cases in the Fort McMurray area. Can you give us a sense of the conditions on the ground at this point? What are you doing to manage risks around that? And I know you talked a little bit about managing your turnaround schedule, if you could flush that out.

Mark Little: Yes. Thanks, Neil. You know, as we've stated before, there's a massive amount of things that we've changed to be able to operate in a COVID world. Everything from bussing, working protocols, masks, sanitization, all sorts of different things, this has been augmented recently with rapid testing. We were part of the Canadian CDL rapid screening consortium. And so, we implemented that. And I would say that, that's now being used across the industry up in Fort McMurray to help in testing asymptomatic individuals. We're finding about 1.4% of the people that are testing positive on -- with our rapid testing and such.

And then from that, just recently, we've been working in collaboration with governments and the communities, and Alberta Health to be able to accelerate COVID vaccinations within the region. I think this is hugely important and certainly would encourage all of the people in Fort McMurray to get vaccinated as soon as possible. But this is a key focus area. And all the companies are working together on coordinating and accelerating rapid testing and vaccinations.

The turnaround -- specifically to your question about the turnaround, part of the issue is there's a number of turnarounds going on within the industry right now. Syncrude's into their big turnaround. Our view was that the labor situation was already stressed. The last thing we wanted to do is over stress that. So, focusing on Syncrude and getting the vast majority out of that way before we started the U2 turnaround made a lot of sense to us, just being able to manage within COVID and such. And we're hoping with acceleration of vaccinations and such, we'll be in a much better situation to efficiently and safely execute the turnaround, and it should actually open up the labor pool. So that's why we've decided to defer.

Neil Mehta: Makes sense Mark, see you in a few weeks.

Mark Little: Thank you Neil.

Operator: And your next question comes from the line of Phil Gresh with JPMorgan.

Phil Gresh (JPMorgan): Yes, Hi, good morning. First question is just on the operating costs. As you've talked about, as you show in your slides, you're expecting those to be pretty flattish for the full year. The first quarter, obviously, was down year-over-year, but we do lap some extraordinarily low OpEx in 2Q and 3Q. So, maybe you could just remind us how you're thinking about the ability to continue to knock out some permanent cost saves versus some of the temporary costs that we'll be lapping that will come back this year?

Mark Little: Ya. Phil, thanks for the question. Clearly, our focus in generating the $2 billion of incremental free cash flow, a lot of this is around restructuring the cost structure of the company. That applies on the ground with things like autonomous haul trucks. But it also affects things like our supply chain. So, we're trying to take a couple of hundred million dollars out of our supply chain, and that's actually been going quite well. It's actually affecting our tailings technologies. So, we're driving down our sustaining capital and some of our ARO by actually using the past technology.

Our supply and trading organization is doing a bunch of work on the trading systems and strategies associated with them. We're expecting to generate a bunch of money out of that as well.

And then we're working on structural changes at the corporate level. So obviously, we are working at this as quickly as possible. You'll get a much better sense when we get into Investor Day because we'll get into the -- how this actually shows up in a little bit more detail associated with it. But we're very confident that we're going to deliver our $1 billion by 2023 and the $2 billion by 2025. So -- and I think that, that's one of the joys that we've continued to invest through this period because it's going to offer ongoing and increasing cash flows.

Phil Gresh: Okay. Got it. And then just on the E&P business, we had oil prices return back -- close to 2019 levels in the quarter, but the cash flows in E&P were still kind of more consistent with what we were seeing last year. So, I was just curious, how would you describe the puts and takes of the performance in E&P? I recognize the production is a bit lower, especially versus 2019. But any other thoughts you could share on E&P? *[call issues]*

Mark Little: I think we lost half of your question, Phil, but let me give it a try, and you can follow up if I don't address your point. I think part of it, we view that we're kind of a pure E&P player associated with it because we really don't care whether production goes up or down. We really don't care what the resource base looks like. We're not short of resource in the company, that's for sure. And so, the focus is making the right decisions at the right time.

Clearly, we're in the process of selling Golden Eagle, and that's just following our disciplined execution process associated with it. Terra Nova is one that we're working to get back online, but nothing's finalized there, and we continue to work with the partners and the government around how that could potentially move forward.

And as Alister mentioned in his comments, we built inventory in the quarter, and so we'll see some of that. So, you didn't see all the cash flow from what we are producing. So, in any particular quarter, it's not necessarily fully representative of the business.

Did that answer your question, Phil?

Phil Gresh: Yes. I mean just -- it seemed like the cash flow was not quite as consistent with a $60 oil period. But I guess, as you said, there are some inventory factors and other things. But -- and I figure currency is also a factor as well nowadays, but I was just curious if there's anything else missing. That was it. Thank you.

Alister Cowan: Phil, maybe I'll just jump in there. The impact of the sales and production and the inventory build is about $75 million in cash flow, just to give you some quantum there.

Phil Gresh: Ok, that is helpful. Alright, thank you.

Operator: And your next question comes from the line of Manav Gupta with Credit Suisse.

Manav Gupta (Credit Suisse): I just wanted to quickly focus a little bit on downstream. What we saw all of last year was Canada managing COVID a lot better than U.S. And it's kind of start of this year, it's flipped a little. U.S. is managing stuff slightly better than Canada. Now you have refining operations in both regions. I'm trying to understand, is Suncor going to be try and sell more products in U.S., now that the demand is looking a little stronger on this side of the border and how you'll manage the situation where suddenly, U.S. demand is looking a little better than Canadian demand.

Mark Little: Yes. Manav, I actually think you've described that quite well is when you look at it, I think what you're seeing is a strengthening of U.S. demand as everyone's coming out of lockdowns. And in Canada, our demand is off. I don't know, in gasoline, it's probably off something like 6% in Western Canada and 17% in Eastern Canada right now. But it's actually going the other way, right? Like we're going into some of the most extreme lockdowns that we've had during the entire COVID. So, you are starting to get this to some degree, a bifurcated market associated with it. What we've been doing is leveraging our logistics to be able to export product into the marketplace. I think that will even be a bigger advantage as the U.S. is moving forward and strengthening further. And so we'll continue to leverage that capability, although in saying that, much less of an issue in the second quarter where we have the inventory now in Canada to cover our turnarounds, and so our utilization will be much lower as we conclude that work. So, I think the timing of our turnarounds is really good in Canada as well.

Manav Gupta: Okay. A quick follow-up, if you could update us on the progress on egress front. We saw TMX getting slightly delayed, and then there's always this issue of Line 5, which keeps coming up. How are you seeing Line 3? So, if you could give us a broader -- your view on the egress situation in Canada, and I'll leave it there. Thank you.

Mark Little: Great, thanks, Manav. You know, on the pipeline situation, Line 3, we expect to come on around this time -- or sorry, by the end of this year around that period of time. Execution timelines are always moving around a bit as it's a bit dynamic. But the confidence and certainty of that line coming on has never been higher.

And if you go to Trans Mountain, Trans Mountain, this is -- I kind of view a lot of this as just normal execution, variability within executing a line. We're expecting that on towards at the end of 2022 and maybe early '23. Those 2 lines add 750,000 barrels a day of incremental egress out of the market. So, this will be very significant to the Canadian market.

And then finally, on Line 5, obviously, this is a significant month because the governor has called for the line to be shut down. We don't think that they have the authority to do that. Obviously, we're working with Enbridge who I think is working very hard and doing a great job of - of keeping the line in service. And one of the things we keep emphasizing both to the northern states as well as into Ontario and Quebec, that if this line gets shut down, it takes half of the oil that flows into Ontario refineries and stops it from flowing there, this will have a consequence on the people in Ontario and Quebec. And I think that the politicians, including the Canadian government are very cognizant of that and working hard to ensure that the laws are followed and that this line stays in service.

Manav Gupta: Thank you.

Operator: And your next question comes from the line of Chris Tillett with Barclays.

Chris Tillett (Barclays): Hey guys, good morning. First, quickly for me. Can you just clarify the numbers you gave again earlier in terms of the buyback figures from April?

Alister Cowan: Yes. So, Chris, in April, we bought $250 million worth of stock back, about 8.2 million shares. So year-to-date, it's just over 20 million shares and about $530 million of -- in dollar terms.

Chris Tillett: Got it. Okay. Thanks. And then, I guess, in terms of your approach there, would you describe it as being more systematic throughout the year and just sort of occurs as the cash flow comes in the door? Or have you kind of front-loaded that? Or just, I guess, generally speaking, where your head is at on that?

Alister Cowan: Chris, it's more systematic. We've just kind of flat lined it. We're not trying to opportunistically time the market. We said we would allocate our cash flow, 2/3 to the repayment and 1/3 to the buyback. And we've taken more of an annual view of that, and we're just systematically going into the market buying back.

Chris Tillett: Okay. That's helpful. Makes sense. And then last for me, I guess, just the figures you highlighted in the presentation about the remaining Oil Sand spend for 2021. I'm assuming a good chunk of that is related to some of the asset maintenance and turnarounds you guys are doing, but can you give us any indication as to how heavy that may be over the next quarter or two versus the shape through the rest of the year?

Mark Little: Yes. I actually think it's fair to say that if you go back and look at it historically, we spend the vast majority of our money in the second and third quarter every year because we try and do all our maintenance essentially between April and October and do as little as possible through the winter period of time. So, you're going to see the vast majority of our capital spend will occur in the next two quarters.

And certainly, with the big turnarounds, that's actually where we're spending a good portion of our money. Obviously, moving the turnaround at Base Plant could push some more of that into the third quarter. But most of the money will get spent in the next two quarters.

Chris Tillett: Got it, ok, thanks guys.

Operator: And I'll now turn the conference back over to our moderator for closing remarks.

Trevor Bell: Great. Thank you, operator. Thanks, everyone, for joining us this morning. If you have any further questions, please reach out to myself and our team here at Suncor, and we'd be happy to answer them. Everyone, stay safe. Thank you.

Mark Little: See you on May 26 or hear you on May 26th!

Operator: And thank you. This concludes today's conference. You may now disconnect.