Bulletin – Energy

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It is impossible to talk about Canadian investing without talking about energy – oil prices in particular. I called the oil price crash based on the fact that the US became a net energy exporter due to fracking and shale drilling technology advancement. Incredibly, three weeks after I called that oil went from well over $100 a barrel to $50 and continued its decline.

Energy isn't going back to previous levels, possibly ever or for a very, very long time. Energy was a good value buy when it was down near $24 per barrel at rock bottom, but it will likely trade sideways, bumping up and down between $40 a barrel to maybe $75 based on world events. Here is what is driving energy prices today – and it isn't demand.

Advancing US shale, fracking, and oilsands technologies

In a bid to survive, "tight oil" producers focused on lowering their production costs. Depending on the company, this is now between $40 and $65 per barrel. This factor will create a ceiling and a floor on prices. As prices fall, they will cut production to reduce losses. As prices rise, they will ramp up production to take advantage of profits (to cover all their debt).

OPEC and non-OPEC nations and their deficits

Saudi Arabia, Russia, Venezuela and other major countries with cheap production costs want higher oil prices, like any producer.

They have announced production cuts to try to remedy this problem and improve their balance sheets, but compliance is weak. This is because they know of this collar on prices due to tight oil which is ready to either come back online or ramp up production. As they can produce oil for around $25 per barrel, and some money is better than none, they know that unless virtually all major oil exporters agree to significantly cut production their reduced production will only have negative effects.

What companies are making money and where to be in energy

Integrated oil companies like the ones you fill up your car with that control retail, pump prices, refining costs, produce the oil you use are a good place to invest if you want energy exposure. Somewhat like a teeter totter, if the price of the oil they are extracting goes down, then their refining units make more money, and provided they control pump costs their margins on refining and fuel sales.

They also pay decent yields between nearly 4% to just over 6%.

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