Energy Investors: Get Ready for Weaker Oil Prices

Description

The price of oil has been on a roller coaster ride since OPEC embarked on its strategy of keeping prices low in order to regain market share by forcing high-cost producers out of the market.

Now there are signs that oil is poised to slip even lower. **Goldman Sachs** claimed that oil could hit US$20 per barrel**.**

Now what?

In recent weeks oil has rallied from the almost seven-year lows hit in August of this year to now be trading at around US$46 per barrel.

Nonetheless, recent data from the U.S. Energy Information Administration is set to put a damper on this rally and indicates that prices will more than likely fall lower in coming months.

You see, despite the U.S. rig count being at its lowest point in over a decade, U.S. oil production has grown by almost 1% since the end of September and is still higher than it was a year ago when OPEC commenced its campaign to push prices lower.

This can be attributed to energy companies continuing to pump crude in order to generate cash flow and remain afloat in the current harsh operating environment.

The sharp collapse of crude has forced energy companies to minimize costs and maximize efficiencies. As a result, they have focused on increasing output from their lower-cost wells in order to boost margins.

For these reasons it is highly likely that U.S. oil output will not fall as sharply as many pundits initially predicted and may, in fact, continue to grow. U.S. stocks of commercial oil are now at their highest point since late April, putting even further pressure on oil prices.

Meanwhile, the demand for crude continues to wane.

Refinery crude inputs remain stubbornly low and are at the same level they were in March, while refinery utilization remains weak. This can only worsen because many refineries are expected to commence seasonal maintenance in the coming months.

Deteriorating economic growth across a number of economies continues to weigh heavily on the global demand for crude, particularly with China's economy in decline. Its third-quarter GDP growth rate was 6.9%, or 30 basis points lower compared with the same period in 2014.

Furthermore, industrial activity for October contracted for the third successive month with no sign of a recovery in sight.

This certainly doesn't bode well for any drop in the global supply glut, which could even grow because Iran is expected to boost output once sanctions are lifted and OPEC has made it clear that it is committed to increasing output over the long term.

So what?

Any further decline in oil prices will have a sharp impact on those energy stocks with weak balance sheets and high operating costs. This certainly doesn't bode well for **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE), **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE) or **Canadian Oil Sands Ltd.** (TSX:COS), which are all saddled with high levels of debt.

Canadian Oil Sands also continues to battle cost blowouts as well as production outages at the Syncrude project, and these are weighing heavily on its ability to reign in operating costs and grow production.

Some analysts highlight the prospects of these companies and the potential upside they offer should oil rally, but with lower oil prices on the way, investors would be better off avoiding these risky investments.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BTE (Baytex Energy Corp.)

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