



## 3 Reasons Why There Will Be Greater Carnage in the Energy Patch in 2016

### Description

If you thought 2015 was a challenging year for the energy patch then think again, because 2016 is set to be even worse. Crude, or more specifically, West Texas Intermediate (WTI), which is the North American benchmark price, has slipped below US\$30 per barrel. At the same time, Western Canadian Select, or Canadian heavy crude, which is the main product of the oil sands, remains under significant pressure, falling below \$20 per barrel as its discount to WTI continues to widen.

These events have already applied considerable pressure to the patch, and there are signs that oil prices are set to fall even further, increasing the carnage.

### Now what?

Firstly, Iran's trade sanctions were lifted over the weekend, and this will increase oil supplies in an already oversaturated global oil market.

Iran has made it clear that once sanctions are lifted it is set to significantly boost its oil output in order to increase government revenues. The country is ready to open the spigots and pump an additional 500,000 barrels of crude daily into a global oil market that is awash with crude and has an estimated daily surplus of up to 2.5 million barrels.

There is already a fleet of crude tankers filled with oil and floating off its coast, ready to sell that crude to global markets. These tankers hold sufficient crude to meet India's import needs for almost a week.

Secondly, there is no sign of any decline in global oil inventories.

Global oil stocks hit a record of around three billion barrels in late 2015, and the International Energy Agency expects inventories to continue growing over the course of 2016.

You see, U.S. oil output remains close to record highs despite the number of operational rigs now being their lowest level in 14 years. Then there is OPEC, with its oil production edging higher as the Saudis and their Gulf State allies are determined to keep the spigots open and pump record amounts of crude.

Finally, global-demand growth for crude is declining.

By the end of the fourth-quarter 2015, the growth in global demand for oil fell by 40% from a peak of 2.2 million barrels daily reached in the third quarter. For 2016 demand for crude is expected to grow on average by 1.2 million barrels daily, which is sharply lower than the rate of growth experienced in 2015.

This means that the growth in global oil supplies is exceeding the growth in demand, exacerbating an already large global supply glut.

All of these factors are applying considerable pressure to oil prices from the supply and demand sides and will force prices lower for the foreseeable future.

### So what?

Clearly, crude prices will remain weak for at least for the duration of 2016, and this in conjunction with WTI set to hit US\$20 per barrel means that the outlook for the patch remains bleak. This, I believe, will lead to a number of bankruptcies and value-eroding capital restructures for a number of deeply indebted energy companies.

Heavily indebted **Pacific Exploration and Production Corp.** (TSX:PRE) is already on the verge of insolvency. As a result, it is now considering restructuring its debt in such a manner that will virtually wipe out investor value. I would expect to see more of these deals over coming months, with **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE), **Pengrowth Energy Corp.** (TSX:PGF)(NYSE:PGH), and **Lightstream Resources Ltd.** (TSX:LTS) among the most vulnerable.

### CATEGORY

1. Energy Stocks
2. Investing

### TICKERS GLOBAL

1. TSX:FEC (Frontera Energy Corporation)

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### Author

mattdsmith

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