When Will Oil Rebound?

Description

Canada's energy sector needs higher oil prices, and fast. Shares of producers such as **Cenovus Energy Inc.,** (TSX:CVE)(NYSE:CVE), **Husky Energy Inc.** (TSX:HSE), and **Canadian Natural Resources Limited** (TSX:CNQ)(NYSE:CNQ) are all down over 30% in the past 12 months. Even majors like **Exxon Mobil Corporation** (NYSE:XOM) and **Chevron Corporation** (NYSE:CVX) are down nearly 20%.

With oil touching below $30 a barrel, more pain may be around the corner as many oil and gas stocks are still being valued on the assumption that oil prices will rise. If oil prices fail to do so, many firms may find it impossible to stay solvent. While many believe oil prices will recover eventually, one question remains: when?

Perhaps not this year

The biggest factor driving oil prices is higher supply, not lower demand. The current supply glut is caused by a few factors. First, the market has been flooded with an unexpected amount of oil from U.S. shale producers. Second, a large amount of supply that was too expensive to develop without $100 oil, such as oil sands, which were brought online during the last bull market. Lastly, major OPEC producers such as Saudi Arabia refuse to cut supply even after prices collapsed.

So, the market has a supply problem, meaning that prices won't correct until production cuts are deep enough to balance the market. Unfortunately, that may not happen until 2017. This week the International Energy Agency released a report saying that unseasonably warm weather and continued rising supplies will keep the crude oil market oversupplied until at least late 2016.

In December OPEC also reaffirmed that it would not cut output to reverse the price slide. "We conclude that the oil market faces the prospect of a third successive year when supply will exceed demand by one million bpd and there will be enormous strain on the ability of the oil system to absorb it efficiently," the agency said.

But oil stocks may rebound in anticipation of 2017

While the oil market may remained oversupplied this year, that doesn't mean investors won't bid up the shares of producers in anticipation of higher prices next year. Famous energy investor Boone Pickens believes this may be the case, especially since most analysts are underestimating how quickly supply may be balanced.

Pickens outlined the previous routs in oil, when the rig count was cut drastically and prices rebounded strongly. In 1998 he said, "Oil dropped to $10 and you cut rigs in half, a 1,000 down to 500. Then the 2001 recession and 2008 recession and they were cut about 40-50%. So, you're going to have the same thing now."

Pickens expects oil prices will return to $90-100 per barrel in the next 12-18 months. His thesis looks to be getting stronger by the day. This week oil rig counts fell to only 650 units, down nearly 70% from their all-time highs. While oil prices may not rebound early this year, a 2017 revival may be right around the corner.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:CNQ (Canadian Natural Resources)
2. NYSE:CVE (Cenovus Energy Inc.)
3. NYSE:CVX (Chevron Corporation)
4. NYSE:XOM (Exxon Mobil Corporation)
5. TSX:CNQ (Canadian Natural Resources Limited)
6. TSX:CVE (Cenovus Energy Inc.)

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Date
2025/06/30
Date Created
2016/01/20
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