How the Latest OPEC Agreement Will Alter the Canadian Energy Industry

Description

After more than half a decade, OPEC decided this week to cap daily production to 32.5 million barrels of oil per day. This represents a drop of 740,000 barrels a day from current production levels.

While the specifics relating to how much each member state will cut production, the impact to the energy industry as a whole could be substantial. Oil prices are still lingering in the mid-US$40 range, where they have fluctuated for over the past few years. Several years ago prices for oil were up over US$100 per barrel.

Why cut production?

Oil-producing companies have been pumping oil consistently for some time now, but that production has been out of sync with worldwide demand, which has fallen in recent years, while overall supply has shot up.

The U.S. in particular has increased oil production drastically over the past few years, which has created a glut of supply on the market and left prices flat.

OPEC in turn has been reluctant to change prices, sticking to current production levels and attempting to weather the storm of low-priced oil. Unfortunately, most OPEC countries are heavily reliant on oil revenues and need oil prices to be at a certain level.

Saudi Arabia in particular has seen a significant decrease in oil revenue over the past few years and was recently forced to not only borrow money from the international bond market, but the country also slashed civil servant wages. The country's growing budget deficit, which hit $98 billion last year, was likely the catalyst to call for this production cut.

What will this do to the Canadian energy sector?

In the short term, this will have little effect.

That being said, the Canadian energy sector is likely rejoicing on this news, and that will send oil prices up (as I write this, oil prices are already up 6%). Alberta as a whole has been suffering from one of the worst economic declines in years, and some additional revenue potential for the energy sector will be more than welcome.

While the increase may not translate into new energy projects for Alberta, the price bump is likely to shore up some stability in prices and help growth.

Over the longer term, the deal is likely to benefit a number of companies, including **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) and **Imperial Oil Limited** (TSX:IMO)(NYSE:IMO).

Suncor is the largest integrated energy company in the country with a diversified portfolio of assets that stem from production all the way down to gas stations across the country. Suncor, however, will be in no rush to restart other projects. The same can be said for Imperial Oil.

Both Suncor and Imperial have significantly cut costs and reduced operations during the past two years of weak oil prices. As two of the largest companies in the energy industry, they both have the resources and capital to withstand prolonged price drops.

Since 2014 Imperial has cut costs by an incredible 35% with operating costs now sitting below $20 a barrel. Suncor too has consistently slashed operational costs in the oil sands down to current levels below $24 a barrel, becoming one of the most efficient low-priced producers on the market.

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