# What Every Investor Should Know About OPEC's Oil Deal

## Description

By now every investor and market pundit is aware of OPEC's recently announced deal to cut production in order to support higher oil prices. This is the first deal that OPEC has brokered since the height of the financial crisis in 2008 when crude plunged to as low as US$31 per barrel. Because of the deal, oil continues to edge ever higher; West Texas Intermediate, the North American benchmark price, is over US$50 per barrel for the first time since June this year.



Nonetheless, it appears that investors are being over optimistic and don't fully understand the deal. There are a number reasons why it won't trigger the massive recovery in crude that some are anticipating.

**Now what?**

The deal is not designed to significantly boost the price of crude, but rather to establish a stable price floor. Cutting output by about 700,000 barrels daily will not have a sufficient impact on the global supply glut where production significantly exceeds demand.

According to one industry insider, OPEC is seeking to stabilize crude prices in the US$50-60 per barrel range. This would certainly ease the fiscal pressures that the Saudis and other OPEC members have been feeling because of sharply weak prices. This makes sense. Riyadh slashed government expenditures to the point where it now needs about $67 per barrel too break even.

There are also issues of who will cut output–cartel members Iran and Iraq remain determined to boost oil output–and how the cuts will be enforced.

Let's not forget that even after agreeing to reduce production, Saudi Arabia slashed its prices for November oil sales to Asia and Northwest Europe. This highlights that the kingdom is still willing to do what it takes to secure market share.

Another aspect that many market pundits appear to have forgotten is the demand side of the equation. Demand is one of the greatest influences on the price of crude. However, demand continues to wane because of the increasing pessimism surrounding the health of the global economy.

Only a month ago, the International Energy Agency, or IEA, revised its outlook for oil prices downward, forecasting lower than expected demand through the remainder of 2016 and into 2017.

There are signs that global economic growth will continue to sputter. There are signs that the Eurozone is facing another banking crisis, as well as doubts over the sustainability of China's growth. These issues have also caused the IMF to revise its forecasts for global growth downwards. It expects global GDP to expand by 3.2% in 2016 and rise to 3.9% by 2021.

Until there is an uptick in global economic growth, it will be difficult to rebalance oil markets to the point where prices will rise significantly.

**So what?**

While the optimism surrounding crude has been particularly infectious, triggering a rally among beaten-down energy stocks, investors should still approach the energy patch with caution.



Regardless of the risks, now may just be the time for investors to test the waters. One of the best opportunities is **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG). Not only has it shored up its balance sheet and reloaded its coffers by recently completing an equity raising, but it has also increased its planned capital spending for the remainder of 2016 and raised its full-year production guidance.

Along with management's expectation that 2017 oil output will also increase, this means that Crescent Point is well positioned to benefit from even a slight increase in oil prices.

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1. Editor's Choice

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