Should You Buy Oil Producers Ahead of the OPEC Meeting?

Description

Oil sector investors are trying to decide if they should hold positions in producers leading up to OPEC's November 30 meeting.

Let's take a look at the reasons why everyone is so focused on the event.

Supply cuts?

The Organization of the Petroleum Exporting Countries (OPEC) has spent most of 2016 telling the market it plans to freeze or reduce production in an effort to boost global oil prices.

The rhetoric helped bring WTI oil up from US$26 per barrel in January to above US$50 in May and June.

With no deal at the spring meeting and reports of record output by Saudi Arabia, the market sold off through July.

OPEC started to get nervous again and ramped up the marketing spin in August, saying it was still keen on putting a supply freeze in place.

Once again, the market bought the story and oil rose back to US$50.

OPEC released a statement at the end of September saying it had agreed to work toward a definitive arrangement by the time the organization completed its next meeting on November 30.

Since then, oil has been somewhat volatile on conflicting reports that a deal is imminent.

Risks

OPEC will almost certainly make a positive announcement on November 30 to avoid a huge sell-off in oil markets, but investors should be careful buying into the hype.

Why?

OPEC members Iraq and Iran have said they want an exemption.

Iraq, which is OPEC's second-largest producer, says it needs to maximize revenue to fund its battles with insurgents. Iran wants to ramp up output as it tries to get production back to full levels after the lifting of sanctions against the country.

This leaves Saudi Arabia holding the bag to reduce output enough to make a difference in the market. That's unlikely to happen given that the Saudis and Iran are supporting opposite sides in regional conflicts.

Even if Saudi Arabia makes significant production cuts, pundits say non-OPEC member Russia would also have to join the pact for there to be any material effect on oil prices.

Russia has said it is in favour of restricting production, but the country is currently pumping oil at record levels, and few analysts expect that to change.

Which oil stocks should you own?

I would avoid the producers altogether, but some analysts believe there is a good chance oil will actually take off in December.

In that case, contrarian investors might want to consider **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG).

The company has managed to increase output while significantly reducing costs through the downturn, and it has a strong enough balance sheet to ride out further weakness.

Production is expected to rise 6-8% next year, and the stock still offers a 2.2% dividend yield that should be sustainable at current oil prices.

If a rally is in the cards, Crescent Point will move significantly higher. If the market doesn't like what it hears out of the OPEC meeting, Crescent Point will slide, but there is little risk of the company going bust.

CATEGORY

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