



Will Oil Reach US\$80 During 2018?

Description

Oil has rallied strongly over the last few months to now be trading at well over US\$60 per barrel. This has been a boon for beaten-down energy stocks with many soaring ever higher as the outlook for crude remains optimistic. Heavily indebted **Baytex Energy Corp.** ([TSX:BTE](#))(NYSE:BTE) has surged by almost 12% over the last three months, while one-time dividend stalwart **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) has added 17%.

In a recent astonishing announcement, global banking giant **Citigroup Inc.** has predicted that oil could reach US\$80 per barrel during 2018. This spectacular forecast flies in the face of the more conservative estimates from the International Energy Agency, the U.S. Energy Information Administration, and investment bank **Goldman Sachs**. All three expect crude to average somewhere between the US\$55 and US\$65 per barrel over the course of 2018.

Benchmark prices West Texas Intermediate and Brent have already exceeded those forecasts as massive inventory drawdowns, supply threats, and growing demand all work to buoy prices. As outlandish as Citigroup's call may appear, there is [every prospect](#) that oil could reach US\$80 per barrel.

Now what?

There are many wildcards that could drive oil prices far higher than expected. Key among these are heightened geopolitical tensions across the globe predominantly triggered by the clash between North Korea and the U.S. as well as the ongoing fiery rhetoric from Kim Jong-un and Donald Trump.

Middle East tensions also remain intense, as Iran and Saudi Arabia continue their proxy war for regional dominance. This, along with terrorism, civil unrest, and separatist movements in Nigeria, Libya, and Iraq, could impact production, possibly shaving over a million barrels daily of OPEC's oil output.

Trump's decertification of Iran late last year has the potential to further disrupt OPEC oil supplies if he elects to reimpose U.S. sanctions. If that occurred, it would likely displace up to 500,000 barrels daily of Iranian oil production.

Meanwhile, Venezuela's (an OPEC member) economy remains in catastrophic meltdown, and its state-controlled oil industry is on the [verge of collapse](#) because of a lack of critical maintenance as well as investment in oil infrastructure and well development. That's caused Venezuelan oil production to plummet by 15% compared to 2016. There are signs that this calamitous decline will continue with the potential to easily slash another 275,000 barrels daily of Venezuela's oil output by mid-2018.

It isn't only supply-side considerations that will support higher crude; there are signs that demand is firming as well.

The likelihood of a further improvement in global GDP growth remains strong because of ongoing fiscal stimulus by a range of governments in major economies, such as the U.S. and China. Trump's tax reform, which slashed the corporate tax rate from 35% to 21% is exceptionally bullish for the U.S. economy and will prompt further corporate spending on expanding operations. Beijing is also bolstering investment in critical infrastructure such as transport networks, which, along with expanding manufacturing activity, will drive greater GDP growth and fuel consumption.

So what?

It is difficult to see oil reaching as high as US\$80 per barrel, but Citigroup's claim certainly has its merits. Given that the global economic environment is at its most positive in a decade, widening supply risks will cause oil to move higher over the course of 2018. That makes investing in beaten-down, higher-risk energy stocks such as Baytex an attractive proposition.

You see, because of its considerable net debt totaling \$1.7 billion, it gives investors significant leverage to oil, yet that debt is manageable because of growing earnings and a well-laddered debt profile. Baytex is free cash flow positive with West Texas Intermediate at US\$50 per barrel or greater, meaning that if oil remains at US\$60 per barrel, the oil company will return to profitability.

CATEGORY

1. Energy Stocks
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