Choose Canadian Oil Companies Wisely: Heavy Crude Discount the Worst in 4 Years

Description

Despite an improving oil-price environment, Canadian oil companies have not experienced the same relative uptick in valuations in recent months due in large part to the widening gap between heavy crude and light crude produced in the U.S. and globally.

This past week, the gap between Western Canadian Select (WCS) oil and WTI oil (the light oil produced by fracking primarily in the U.S.) widened to a four-year high. This gap has provided a number of iconic Canadian oil and gas producers with headwinds, despite headlines that oil is on the rise.

With oil priced in U.S. dollars, a weakening Canadian dollar would therefore provide a reprieve for many producers. The strengthening Canadian dollar and correspondingly weakening greenback has provided yet another headwind many Canadian producers are currently battling.

In this environment of multiple headwinds facing the Canadian oil sands, investors have begun to consider diversification with the oil and gas firms selected to be portfolio mainstays. I have suggested Canadian investors looking for exposure to companies traded on the TSX in the oil and gas sector look to highly diversified companies, such as **Suncor Energy Inc.** (TSX:SU)(NYSE:SU), or companies with significant global operations, such as **Parex Resources Inc.** (TSX:PXT).

While one could argue that this gap between heavy and light crude may be short-lived, providing a buying opportunity for aggressive value investors in Canadian oil sands operations, I don't see this trend dissipating for some time due in large part to the changing fundamentals of the oil and gas industry. Canadian heavy crude is still almost entirely refined in the U.S., and with transportation costs increasing due to the need for increased pipeline capacity, which is still a ways away, investors can rest assured that a significant price gap will continue in the medium term.

Fellow Fool contributor Ryan Goldsman recently suggested investors consider Canadian oil companies **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) and **Baytex Energy Corp.** (TSX:BTE)(NYSE:BTE) as two plays Canadian in the oil and gas space. However, I believe these two companies are likely to fall victim to many of the headwinds I've mentioned due to their relative exposure to WCS and AECO oil. I re-affirm my confidence in Suncor and Parex as better long-term plays for commodities investors looking for exposure to the oil and gas sector.

At this point in time, it is important for investors to dig deeper into the financials of oil and gas companies to select those that are likely to outperform over the long run. A rising WTI or Brent crude price does not mean Canadian producers will profit evenly.

Stay Foolish, my friends.

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2. NYSE:SU (Suncor Energy Inc.)
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Author
chrismacdonald