Why Canadian Energy Stocks Are Struggling

Description

The past few years have seen hard times for the Canadian energy sector. After more than a decade of rising oil prices and seemingly endless economic progress in Alberta, the energy sector came crashing down in 2014, with a steep, abrupt fall in the price of oil. Oil prices have still not returned to their 2014 levels, and although they've risen somewhat on average, the energy sector has been sluggish since then.

The year 2018 was a particularly weak year for energy stocks, with many posting losses or seeing earnings fall year over year. The question is, why? With **BP** having recently posted its best earnings in five years, we have proof that low oil prices needn't necessarily drive energy stocks down. But the Canadian energy sector remains weak. To understand why, we need to look all the price of oil–not in aggregate, but Canadian oil specifically.

Persistent weakness of oil

It's normal for people speak of the price of oil or per barrel cost of crude, but technically there is no one universal oil price: various types of oil from various places have various prices. For example, as of this writing, Brent Crude was $62 a barrel, while Western Canadian Select was just $43. It's the latter type of oil that Canadian energy companies sell, refine and process, so Canadian projects bring in less from a barrel of crude sold than a company like BP does.

Why is Canadian crude so much cheaper than Brent? It has to do with ease of processing. Canadian crude comes mostly from tar sands, resulting in heavy crude that requires extensive processing before it can become economically viable. All that processing costs time and money, so companies involved in processing Western Canadian Select incur great costs to process cheap oil. So although Western Canadian Select is cheap, it's also low margin and generally less profitable to sell compared to, say, OPEC oil. The end result is that Canadian oil projects earn less than Saudi ones. This creates a spillover effect impacting the entire energy sector, even companies that are not directly selling or processing crude.

Project delays

Another factor harming the Canadian energy sector right now is project delays. Many Canadian energy companies, like **TC Energy** (TSX:TRP) are involved in building pipelines to transport oil to the United States. These pipelines are lucrative when they get the go ahead. The problem is, they don't always get it: TC's Keystone XL has been blocked numerous times by officials in the States, most recently by a Montana judge who blocked a segment of the pipeline because it hadn't been vetted enough for environmental impact. The decision is being appealed, but a long delay is inevitable.

Not all energy stocks are created equal

Despite the overall doldrums in the energy sector, not all energy stocks are doing poorly. Utility companies, for instance, are generally doing quite well: **Emera Inc** grew earnings by 30% in its most recent quarter, and is up about 6% over the last 12 months. It makes sense that utilities would dominate the energy sector, as many of them rely on renewables like hydro, and aren't as vulnerable to the price of oil. This makes them better buys in sluggish markets than conventional oil and gas stocks.

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Date
2025/07/27
Date Created
2019/02/09
Author
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