3 Oil Stocks With Less Risk

Description

Oil stocks have been fraught with risk in recent years.

After a decade of rising oil prices — albeit with some bumps along the way — surging supply caused prices to crater from US$100 per barrel in 2014 to around US$60 per barrel today. Volatility has become the norm.

While there certainly aren't any guarantees in commodities investing, there are ways to manage your risk exposure. Purchasing diversified, integrated oil companies is an ideal way to remain exposed to upside while mitigating your downside.

Here's how it works

The biggest advantage integrated oil companies have is that they have assets throughout the value chain. They often drill for oil, refine their output, transport it to market, and sell it to end users.

For comparison, other companies only focus on one specific function, making them reliant on competitors and market forces for the rest.

A great example of how integrated oil companies can weather volatility involves their refining arms.

Refining margins, referred to as "crack spreads," often run counter cyclical to oil prices. During rising oil prices, crack spreads narrow. When oil prices fall, profitability rises.

So, while most producers are crushed after oil prices drop, integrated companies get a well-needed cushion using the profits from their refining operations.

Which oil stocks display this level of risk management? Here are three integrated oil stocks that warrant your consideration.

Suncor Energy (TSX:SU)(NYSE:SU)

Suncor is an integrated energy company based in Alberta. Specifically, it focuses on synthetic crude production from oil sands projects.

Recently, Warren Buffett purchased nearly 1% of the company's shares. Why? Likely because of its refining arm.

"Suncor has a strong downstream operation, which financially benefits from oil bottlenecks and that is unique to Suncor, which you can't get with many other companies in the energy space," commented a portfolio manager at **Manulife**.

Husky Energy (TSX:HSE)

While Husky's oil production has dipped recently, management credits its refining arm for churning out plenty of free cash flow.

"This further demonstrates the value of our Integrated Corridor business," Husky's CEO said. "We can capture value at any point along the Upstream-Downstream chain, resulting in global pricing for most of our production."

Refining profits are a huge advantage considering oil sands output typically warrants a $5 discount on the open market. To make up the difference, Husky is able to buy its own output on the cheap, process it through its refineries, and fetch a global price for its output.

No wonder that the company's CEO credits refinery margins as one of its greatest value adds.

Imperial Oil (TSX:IMO)(NYSE:IMO)

When the Alberta government enforced mandatory production cuts across the region due to oversupply, Imperial's CEO was furious. He called the action a "drastic, dramatic manipulation in the market."

It's no wonder he was upset, as Imperial wasn't nearly as impacted by the market's oversupply compared to its competitors.

Last quarter, it produced 388,000 barrels per day of oil. Its refineries processed 383,000 barrels per day, covering nearly its entire output. Meanwhile, its petrol stations sold 477,000 barrels per day.

Imperial Oil controls the entire value chain of oil, giving it offsetting revenue streams in any market conditions.

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