Energy Shares Offer Investors 2 Smart Pre-Recession Plays

Description

Taking a contrarian position is no easy task: It's one thing to see the opportunity, but another to actually place a bet on it.

However, energy looks ripe for exactly this kind of play, with stocks across the sector looking oversold and an array of unfashionable stocks offering value opportunities for those with the guts to buy into them.

Furthermore, a moderate view of the economy suggests that energy will briefly become all the rage – just before a deep recession.

The next downturn could be preceded by sharp energy upside

It's arguable that recession follows a predictable pattern – and that investors do, too. Macroeconomists will point out that recession is preceded by inflation and a dangerously bullish sentiment that overheats the markets.

Traditionally, the rally follows a spectrum of assets, starting with gold and silver and culminating in energy. What this means for energy investors is that there could be a window of big upside just before the spectre of negative GDP strikes.

An investor will have to time it right, though, or risk ruination. One reason for this is that stocks – while cheaper than perhaps they should be – are today trading at higher prices than they did before the 2008 crash.

In other words, the losses incurred could be relatively greater than those during 2008. And that's where energy stocks come in.

Rising inflation could signal the time to sell

While shorting the energy stocks when the market turns sour would of course add to the problem, the strategy of buying when nobody else is and selling before everyone else does is the perfect contrarian play.

That's why watching inflation levels is key. Stocks that are cheap today, such as **Tourmaline** (TSX:TOU), are ideal targets, while **Enbridge** (TSX:ENB)(NYSE:ENB) could simply be bought at a knock-down rate today and held throughout a correction.

Tourmaline is a great play for value, it has to be said, though its price volatility has been rather high of late – perhaps too high for the subtle tastes of a low-risk investor even if it is trading at an all-time low.

Its market fundamentals beat the oil and gas industry, though there's still the possibility that the share price will fall even further. Coupled with a strong track record and a healthy balance sheet, there's a lot to recommend this stock to a value investor.

Enbridge, on the other hand, could provide two functions here: Investors could cash in once inflation hits its peak, or hold on throughout the ensuing recession for some defensive dividends in a classically safe asset type.

Indeed, if key developments in the Trans Mountain region are forthcoming, Enbridge could soar higher than most, making that sell-or-hold decision mid-inflation all the more difficult to call.

The bottom line

Recession is becoming a very real possibility if a growing number of pundits are to be believed, though the classic pattern of economic cycling holds that inflation must first run its course.

This gives energy investors a strategy that they can use to glean some upside before a correction, with beaten-up oil and gas stocks like Tourmaline providing the widest profit margin, and stocks like Enbridge providing security.

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