Why Inter Pipeline (TSX:IPL) Stock Just Doubled in Price

Description

Inter Pipeline Ltd (TSX:IPL) stock was crushed by the market collapse. In January, the stock was priced at $22. On March 18, the price fell below $6.

Then something incredible happened. In just a few weeks, the share price *doubled*. There's now a feeling that the stock could retest its pre-pandemic highs, which would still represent an additional 100% in upside.

Is there still time to profit by buying Inter Pipeline stock? To figure that out, we need to determine why shares have been so volatile in the first place.

Inter Pipeline was promising

Inter Pipeline bills itself as a "top tier energy infrastructure business that has significant growth potential." How true is that statement? As with most company marketing, the reality is a mixed bag.

There's no doubt that the company owns some incredible assets. Pipelines in particular have proven to be an incredible investment. That's because in recent decades, North American fossil fuel production has surged. All that output needs to be transported to refineries and end-users. Pipelines are the fastest, cheapest, safest option.

But there's a mismatch. Fossil fuel production can ebb and flow on a daily basis. Pipeline infrastructure, meanwhile, takes years to build. Surging production and slow pipeline construction times have resulted in a capacity shortage in Canada for nearly a decade. If you already own a pipeline, your pricing power has shot through the roof. That's good news for Inter Pipeline shareholders.

Time to buy?

Pipelines are good business, but despite its name, Inter Pipeline derives only 15% of its income from conventional pipelines. Another 30% of its business is either natural gas processing or bulk liquid storage. The remaining 55% is considered "oil sands transportation." This is where the trouble starts.

Oil sands transportation includes a fair amount of pipelines, but this segment is broken out because oil sands operate on very different economics. Whereas shale oil projects can break even at prices below US$20 per barrel, oil sands companies often need prices to surpass US$40 to turn a profit. That's *double* the current price.

The long-term pressures are clear. The longer oil prices remain depressed, the more likely it is that Inter Pipeline's customer base will shut down operations. Energy producers will only pump at a loss for so long. Eventually, Inter Pipeline could see major revenue sources exit the market *permanently*.

As mentioned, when volumes are rising, owning and operating a pipeline is terrific business. But when volumes fall, the high fixed costs of maintaining the infrastructure could push a business into loss-making territory quickly. That's what Inter Pipeline investors were terrified of when the stock fell below the $6 mark.

Oil prices have recovered a bit in recent weeks, but they're still nowhere close to justifying the 100% rise in Inter Pipeline's stock price. More than half of its customer base is generating daily losses. This will continue to be true even if oil prices recover by an additional 50%.

There are some fantastic stocks worth buying following the market crash. Inter Pipeline isn't one of them.

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