Why Enbridge (TSX:ENB) Stock Dropped 26% This Year

Description

Enbridge (TSX:ENB)(NYSE:ENB) stock used to be a reliable winner. From 1995 to 2015, shares rose by 1,700%. Dividends pushed the total return to nearly 2,000%.

Then something strange happened. Over the last five years, shares have been stagnant. In 2020 alone, the stock is down 26%.

What's going on? It's turns out that the truth is shocking, and that it's much bigger than Enbridge alone.

Prepare for the truth

Oil is dying. Few people are willing to accept this fact, but it's true. Just ask one of the largest oil producers in the world: **BP**.

"Instead of forecasting continued consumption growth, the oil company now believes that demand has peaked and will decline even in a best-case scenario," reported Fool contributor Matt Dilallo. "It's a chilling forecast that has reframed how BP plans to operate in the future."

A peak in global oil demand would crush Enbridge. The company is the largest pipeline operator in North America. It transports roughly 20% of the continent's crude oil and natural gas. Most of its revenues are directly tied to volumes. If oil drops, cash flow falls.

But there's an even bigger problem. Enbridge is a high-fixed-cost business. That means it must pay a huge sum to maintain its vast infrastructure *regardless* of what revenues are.

This dynamic means that a fall in revenue can have a disproportionate effect on profitability. If sales fall 5%, profits might drop by 20%. That's a scary position to be in if oil demand has truly peaked.

Where will Enbridge stock go?

Why has Enbridge stock remained stagnant for five consecutive years? Because oil prices have fallen from US$100 per barrel to just US$50 per barrel over that time period. That made the market nervous about its customers' financial viability. If the customer base goes bankrupt, volumes would be disrupted.

The fall in 2020 is a different beast. This time, the market is worried the entire game is finished.

"If the recovery from the pandemic is slower and there's lasting economic damage, oil demand may only have a couple of years left to grow," the IEA said. That forecast falls roughly in line with BP's predictions.

"The outlook from the agency, which advises most major economies, comes as oil majors like BP and **Royal Dutch Shell** acknowledge that combination of the pandemic with and the drastic changes required to avert a climate crisis will have profound consequences for their assets and business models," added *Bloomberg*.

Enbridge needs steady oil volumes to maintain profitability. A slight dip would put its entire business model in doubt. Worse still, the company is moving forward with massive expansion projects that will take a decade or more to pay off. If oil demand is indeed falling, these may ultimately prove to be stranded assets.

Many investors are jumping into Enbridge stock, arguing that this year's plunge is a buying opportunity. Fossil fuel stocks, however, are ticking time bombs. That should keep a tight lid on valuations.

Yes, Enbridge stock looks cheap, but there's no reason to believe it won't remain cheap forever.

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