Will Energy Stocks Tank if War Pushes Oil Prices to US$100 or Higher?

Description

Simple economics say that the law of supply and demand dictates the price of a product. The same law applies in the energy sector, specifically to oil. If you recall, 2020 was a forgettable year for oil companies. Russia and Saudi Arabia engaged in a price war on March 8, 2020.

The COVID-19 pandemic compounded the problem and caused a massive decline in demand. Because of the glut or oversupply, Brent crude oil prices tumbled to less than US$10 per barrel and WTI plunged to negative US$37 per barrel later on. In 2021, crude prices rebounded because demand outpaced supply.

Fast-forward to the present and we see oil prices inching closer to US$100 per barrel. However, a potential military conflict is the trigger, not necessarily demand. The Russia-Ukraine border crisis has turned from bad to worse. Russian President Vladimir Putin signed an order to send troops to two breakaway areas of Ukraine.

War is the bigger threat to the markets than rising inflation. It could dampen investors' sentiment and cause stocks to fall, including constituents in the red-hot energy sector. Investors holding shares of **Enbridge** (TSX:ENB)(NYSE:ENB) or **Imperial Oil** (TSX:IMO) may be less nervous.

Fear factor

Oil prices are spiking in recent days due to fears an invasion in Ukraine would result in disruptions on the supply side. But with troop deployment or invasion starting, the disruption in crude supplies would be global. The U.S. and Europe could initiate economic sanctions against Russia, the world's second-largest oil producer.

Besides the geopolitical tension, the normalization of the global economy post-Omicron could also create an imbalance between demand and supply. Peter Cardillo, chief market economist at Spartan Capital Securities, say the market is going to stay in a state of confusion as long as the fear factor is elevated. Analysts are clueless as to Putin's next moves.

Energy majors

Enbridge belongs to the energy industry but has endured the tailwinds and perennial volatility for decades. The $83.46 billion energy infrastructure company operates more like a utility company, and therefore, the business model is low-risk. Its four blue-chips franchises are gas distribution, gas transmission, liquids pipeline, and renewable power. All have organic opportunities ahead.

Enbridge pays a lucrative 6.56% dividend, and has 27 consecutive years of dividend increases. With a $19 billion secured capital plan, management expects the business to grow 5% to 7% (CAGR) through 2024). If you invest today, the share price is $41.18 (+7% year-to-date).

Imperial Oil is also a reliable income provider. The $37.25 billion crude oil and natural gas producer is nearly half the size of Enbridge, but its dividend track record is about 14 decades. It boasts a dividend growth streak of 26 straight years. Management raised the yield recently by 26%.

While this energy stock pays a smaller dividend (2.45%) than Enbridge, the stock outperforms. At $55.40 per share, current investors are up 21.4%. Based on market analysts' price forecast, the maximum return potential in 12 months is 26.4% ($70).

Guarded optimism

The energy sector will continue to be the best performer if the oil pricing environment remains favourable. However, a broad-based market decline or severe correction due to war could send energy stocks tumbling too.

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