Oil Finally Crashed: Is the Party Over?

### Description

This month, the price of oil crashed, falling from a peak of $123 to a low of $102.80 — a 16.2% decline. WTI crude prices were impacted by a number of factors this month, including the U.S.'s strategic petroleum reserve (SPR) release, and Joe Biden's planned meeting with Saudi leaders. Both of these factors have the potential to increase the supply of oil. So, futures traders are naturally betting on lower prices.



So far, these bets are paying off. Not only is crude oil down in the futures markets, but gasoline is going down in the real world. So, there are some signs that the energy crunch is easing. But is the party in oil stocks really over for good?

## Why oil crashed

There are a few factors that may have contributed to the crash in oil prices this month:

- Rising interest rates
- The U.S. SPR release
- Joe Biden's planned meeting with Saudi Arabian leaders

Rising interest rates should theoretically reduce the demand for oil. The other two factors above may increase the supply. The U.S.'s SPR release is definitely adding supply to the market, Biden's meeting with the Saudis may do so if it is successful. All of this combined is giving investors the sense that it's time to cool it with bullish bets on oil.

## Is the party over?

If you just got into energy stocks like **Cenovus Energy** (TSX:CVE)(NYSE:CVE) recently, you might bemoan the bearishness in oil prices this month. Those who bought oil stocks early are still sitting on huge gains, but investors who joined the party late are hurting.

So, is the party in oil stocks over?

Nobody knows for sure, but my feeling is "probably not." Many oil stocks remain undervalued today, even if you assume the price of oil will be sub-$100. If you look at Cenovus, for example, it trades at just six times forward earnings and eight times operating cash flow. Even after its monster rally this year, it's still extremely cheap. If oil prices fell a lot, maybe the free cash flow multiple would rise to 10. But this is still cheaper than your average stock.

Analysts seem to be underestimating the earnings implications of the kinds of oil prices we're seeing today. Even at $100 oil, companies like Cenovus are likely to beat expectations. So, there is plenty of room for optimism.

## Foolish takeaway

There's no denying that oil prices took a beating last week. But there's also no denying that oil stocks are still cheap. We may not see oil prices go higher and higher forever, but that doesn't mean that oil stocks aren't great buys. Even with oil at $100, they will generate very high profit margins.

These days, there are many factors holding back the supply of oil. Perhaps they can be eased somewhat, but it doesn't look like we're heading back to 2020 or even 2021 prices anytime soon. The world has emerged from its COVID-19 era slump, and people once again have energy needs.



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