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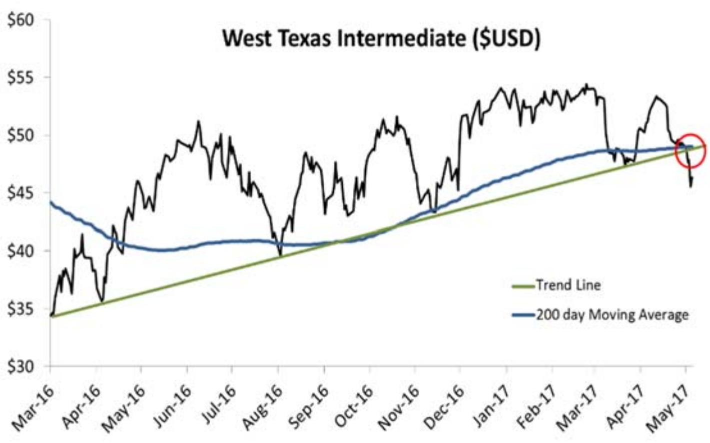
Does this Feel Familiar?

Most of us clearly remember the happy days in mid-2014 when West Texas Intermediate (WTI), the standard measurement for the price of oil, was merrily trading at $107 per barrel. The largest concern for many Calgarians was whether to buy the 60 inch or the 80 inch television for their new entertainment centre. By the middle of January, 2015 the price declined over 58% to $45 per barrel. It marked the beginning of a difficult time when thousands of people lost their jobs and billions of dollars were lost in the energy sector. To put the loss into perspective, WTI dropped over 11% on average every month for seven and a half months.

Just three short weeks ago WTI was trading almost 13% above current levels! More harm than good is typically done by projecting short term moves into the future, but when we couple this with the fact that WTI just broke down through a couple of important technical levels, including the 200 day moving average, there is some cause for concern. Don't panic, it could very well be that this is merely a short term dip and a rally is imminent. Hopefully today's two percent bounce is indicative of that, but we would like to explore how we are positioned in the event that this is not the case.



Source: Bloomberg

In 2014, just before the crisis began, our top two energy holdings in the QV Canadian Equity Strategy were Suncor and Canadian Natural Resources. Our current energy holdings illustrate our continued confidence in these two companies as they still account for two of our top three energy positions. We added AltaGas, an energy infrastructure company, to the strategy in May of 2016 and recently bumped it to the top spot of our energy holdings.

Both Suncor and Canadian Natural Resources are among the lowest cost operators in their peer group, providing them with greater ability to remain profitable if commodity prices drop. During the last crisis this allowed them to generate more cash flow as other companies were forced to sell assets at steep discounts. Canadian Natural Resources used the cash flow to improve existing operations whereas Suncor took direct advantage of this by purchasing a controlling stake in Syncrude near the bottom of the cycle. During their 2016 annual general meeting, Suncor's CEO, Steve Williams, was quoted saying, "Right now I can buy on the market facilities that are operating for the same or less price than we could build ourselves." Both companies own long life assets that do not have the steep production declines of traditional oil and gas production. Furthermore, these management teams have experience in utilizing energy downturns to their advantage.

Alternatively, AltaGas provides energy diversification because almost all of its profitability is utility-like in nature with prices that are contracted or regulated. AltaGas' spot price exposure has diminished significantly in recent years and its sustainable dividend yield of 6.7% should also provide downside production in troubled markets. Negative sentiment has improved its valuation and the completion of a major project in 2014, Forrest Kerr, has decreased construction risk in the meantime.

While the TSX Energy Index is down 30% since mid-2014, Suncor and Canadian Natural Resources have weathered the downturn by shedding only nine percent and 13% of market value, respectively. At a loss of 35% during the same time, AltaGas' price performance was more challenged, but we believe it is in a much better position today. These three holdings comprise over 70% of our energy exposure. Although we remain hopeful that a better energy environment is on the horizon, the strength of these businesses allows us to sleep soundly at night without knowing what might be in store for the future.