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Oil Is on Another Steep Slide, but Stocks Don't Care

Oil has less of a drag on stocks--as long as it stays over $40 a barrel

By
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Oil prices are on track for one of their biggest weekly drops since January — yet stocks don't seem to mind.

At the start of the year, equities and oil prices appeared to move in lockstep, with the S&P 500 often trailing crude.

But since Monday, the West Texas Intermediate crude benchmark has fallen close to 7% and U.S. stocks are poised to cap the week with gains. As the price of oil whipsaws, equity market volatility is hovering around two-year lows.

Even shares of energy companies have barely budged. The S&P 500 energy sector is on track to end just 0.3% lower, while European oil and gas companies added 0.7%.

Analysts have several theories for the untangling.

While oil has been volatile this summer, front-month contracts for both Brent, the international oil benchmark, and WTI are still up over 60% from their lows of the year. Few analysts expect them to retest those sub-$30 levels anytime soon.

“People got used to the idea that oil is likely to be relatively volatile, but within a sort of $40-60 a barrel range,” said Mike Bell, strategist at J.P. Morgan Asset Management. Above that range, supply comes back into the market, forcing prices to retreat, he said. When oil heads lower, though, producers cut, pushing the price higher again, analysts say.

That $40 to $60 range isn’t great for energy companies, but it is unlikely to threaten the sort of corporate debt defaults that sent markets into a tailspin earlier this year. Those prices are also unlikely to force sovereign wealth funds in oil dependent nations to sell their investments to make up for lost profit, analysts say, which has put pressure on equity markets before.

“Oil doesn’t seem to be a big drag on the market until it drops below about $40,” said Randy Frederick, director of trading and derivatives at Schwab Center for Financial Research in Austin, Texas.

That’s a level where many companies in the fracking industry start to cut jobs or risk defaulting on their debt, creating stress in U.S. high yield debt, he said.

Other investors may simply be too shell-shocked from January and February to care, now viewing oil price fluctuations as part of a supply-driven, speculative market that is disconnected from the global economy. “You get a bit of panic exhaustion,” Mr. Frederick said.

Some investors may also be taking comfort in near-record net long positions on oil which have built up this week, according to Neil Passmore, chief executive at Hannam and Partners, which advises companies.

“The crude swings are volatile, but there’s still a consensus long and an equity market that says we’ve been here before, and we’ll be a bit more relaxed about it,” he said.