

# Energy investing without macro calls

March 2026

## Bottom line up front:

- **Oil prices are notoriously unpredictable**, swinging from surplus to shortage in short order—making short-term forecasts unreliable and often counterproductive for investors.
- **Despite near-term volatility, long-term oil prices are far more stable**, anchored by producer cost structures that act as a gravitational force over the cycle.
- **Our primary investment edge comes from underwriting investing businesses, not barrels**—focusing on cost curves, capital allocation discipline, and management quality to turn volatility into opportunity.

Oil has a way of humiliating forecasters. Just three months ago, prices hit a four-year low of roughly \$55 per barrel amid meaningful oversupply. Recently, concerns about an impending shortage have pushed prices above \$100, and some headlines suggest \$150 may not be far behind.

This whiplash can be difficult to navigate. Many investors chase momentum—buying high out of fear of missing out—only to sell after the pullback. Others freeze when uncertainty rises, unsure which signals matter and which are simply noise. Given that backdrop, we're often asked a version of the same question: **How can a bottom-up value firm make long-term investments in a sector as volatile as energy?**

It isn't because we believe we can predict short-term price gyrations. As bottom-up investors, we rarely take a view on macro variables—much less one as complex as near-term oil prices, which must continuously reconcile inventories, OPEC policy, demand conditions, and geopolitical risk. In our experience, consistently forecasting that combination is extremely difficult—if not impossible.

Real oil prices vs. 5, 10, and 25-year historical averages



Data Source: Inflation-adjusted oil prices were calculated in-house using Crude Oil Prices: West Texas Intermediate (WTI) - Cushing, Oklahoma and Consumer Price Index for All Urban Consumers (CPI-U) data sourced from FRED, the Federal Reserve Bank of St. Louis, as of 3/17/26.

Paradoxically, though, this short-term volatility often causes investors to overlook far greater long-term stability. While spot prices can move dramatically over a year—or even a month—average prices over longer periods tend to fall into a much narrower range. Adjusted for inflation, the average oil price has been broadly similar whether you measure the past 5, 10, or 25 years.

That stability is not incidental. Over the long term, oil prices are governed by the cost structures of the producers. If oil prices are so low that producers can't profitably drill, they reduce activity until the market is undersupplied. Historically, if prices are high enough for producers to earn excess returns, they increase activity until the market is oversupplied. These producer economics are far more stable than the daily oil price quote. Over the long term, they act as a gravitational pull on oil prices.

This logic underpins our valuation of oil companies. We can't predict how oil prices will move in the short term, but we can understand the producer cost structures. Think of it as our bottom-up approach to estimating a top-down variable.

The mid-cycle oil price, of course, isn't the only variable we underwrite. Our primary focus is on underwriting businesses, not barrels. Factors like operational efficiency, asset quality, inventory depth and balance sheet strength are all critically important. In fact, one of the most important considerations in underwriting an oil investment has little to do with the commodity price: capital allocation.

There are few sectors where management teams are required to redeploy as much capital, and as quickly,

as in energy. For the median S&P 500 company, management might reinvest 40% of its market capitalization in the next five years. For upstream energy companies, that figure can easily exceed 100%. When management is tasked with reinvesting the entire market cap over our holding period, the quality of those investment decisions can matter more than the oil price.

For that reason, we place particular emphasis on management quality in the oil industry. We focus on managers that have a disciplined capital allocation framework and a track record of creating value through the cycle. This has often worked in our favor. ConocoPhillips, for example, created enormous value for owners through opportunistic acquisitions near the bottom of the COVID price cycle. EOG has similarly compounded value over the years through long-term, high-return organic exploration. In midstream, Targa Resources has created value by pulling both levers—accretive acquisitions and high-return organic investments—while also returning capital through share repurchases.

Stepping back, we may not have an edge in predicting oil's next move, but we believe we do have an edge in underwriting businesses—what they can earn through the cycle, how they allocate capital under uncertainty, and what we are paying for that stream of cash flows. With that steady view of value, oil price volatility becomes less about risk and more about opportunity.

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GEN-5060