Record-low Canadian crude price is a clue that oil sands' best days are past

By Barrie McKenna
November 16, 2018 – *The Globe and Mail*

Prime Minister Justin Trudeau told a gathering of oil executives in Texas last year that, "No country would find 173 billion barrels of oil in the ground and just leave them there."

The logic was sound when oil sands crude was selling for US$50 or US$60 a barrel. It's a lot less obvious after the price touched a record-low of less than US$14 a barrel this week.

Canadian crude has become the most discounted oil on the planet. The price collapse is a decidedly bad omen for Canada's oil patch, and the broader economy.

At today's prices, no one wants to extract the heavy oil buried deep in the ground. Some desperate producers would rather curtail output than sell oil at these bargain prices. A clutch of major Canadian oil sands producers – including Cenovus and Canadian Natural Resources – are begging Alberta to order an industry-wide production cut to boost prices.

The chronic price gap between Western heavy crude and the North American benchmark, West Texas Intermediate, has grown to $40 a barrel in recent months, up from a typical spread of $15, costing the economy tens of billions of dollars.

Perhaps we could all just chill if the current depressed price was only a temporary blip, caused by transportation bottlenecks. Proposed pipeline projects, such as the Trans Mountain expansion and Keystone XL, would eventually ease the short-term price pressure.

But limited rail and pipeline capacity is not the only dark cloud on the horizon. The broader challenge is that Canada finds itself in the unenviable position of being the high cost producer in a world awash in oil.

Many large foreign players apparently saw the future, and have already fled, unloading billions of dollars in Canadian oil sands assets. Royal Dutch Shell, Marathon, Statoil and ConocoPhillips were all big sellers in 2017, leaving mainly Canadian-based producers in the oil sands.

Back in the early 2000s, the global oil industry saw the vast reserves buried in Alberta and Saskatchewan sand as essential to their future. The logic was that with dwindling reserves, even costly and technically challenging oil would eventually be needed. All the major global players wanted in.

Two factors have turned that reasoning on its head – the U.S. shale oil revolution and greenhouse gas emissions.

Hydraulic fracturing technology has made Canadian crude less essential than ever – a risk producers should think about as they consider shutting off the tap. Fracking has given the world an abundant new source of oil and gas that is relatively cheap to extract, and easy to turn on and off as prices fluctuate. Oil sands projects, on the other hand, can take nearly a decade from conception to production. The heavy crude they make is also more expensive to refine. And the oil sands, located far from consumers, is condemned to the role of price-taker in this uncertain energy market.

The other obvious challenge is climate change. Oil sands crude is both high cost and energy intensive. Looming carbon taxes and emission restrictions are strikes against the industry.

Corporate social responsibility is not killing the oil sands, as some critics have suggested. Investors everywhere are re-evaluating – and repricing – climate risk. And when they do the

math, the assumption that oil sands production will continue rising no longer seems inevitable.

So, yes, more pipelines would help. It's not like key players, including political leaders and chief executives, aren't doing everything they can to get them built. The federal government, on behalf of Canadian tax payers, is investing nearly $12-billion to purchase and expand the Trans Mountain pipeline to get Alberta crude to foreign markets. Likewise, TransCanada Corp. insists it isn't giving up on the Keystone XL pipeline, even after a federal judge quashed a U.S. presidential permit earlier this month.

The price malaise hanging over Canadian heavy crude won't miraculously clear if one or both of these pipelines is approved. Nor will a forced production cut save the industry.

Canada produced a record 4.2 million barrels a day of oil in 2017, and is on a course to grow that to 6.2 million barrels a day by 2035.

Today's rock-bottom prices are a warning that the industry may never get there, and that the oil sand's best days are already in the rear-view mirror.