Energy Expert Jeff Rubin on Why the Cost of Shipping Oil By Rail Is Poised to Rise

Description

In the final part of my interview with author and former CIBC Chief Economist Jeff Rubin, we discuss how regulations following the recent tragedy in Lac Megantic, Quebec could impact **Canadian National Railway** (TSX: CNR, NYSE: CNI) and **Canadian Pacific** (TSX: CP, NYSE: CP). Below is the transcript of our conversation; it has been lightly edited for clarity.

Robert Baillieul: This was probably just an amusing sideshow, but Neil Young was in the headlines for his criticisms of the Keystone XL pipeline and the oil sands.

Jeff Rubin: Well, probably that goes over as well in Alberta as “Southern Man” went over in Mobile, Alabama. But I don’t really care what Neil Young thinks about the oil sands.

Here are some of the issues to think about. The environmental issues are more complex because of the way the industry responds. Stopping pipelines was originally intended to limit production and keep the oil underground. I certainly see that as a legitimate view to have, particularly when we hear that we’re already at 400 parts per carbon. But we’ve got to realize that in the real world, the oil industry is going to respond. The rail industry is looking for new business and is going to respond. Somehow, when we do things, the impact of that comes out perversely.

I think the real issue now is, if I were in the environmental movement I’ve got to switch my focus to rail. Like Harrison was saying at Canadian Pacific, the regulator has got to get up to speed here because there hasn’t really been any oil/rail regulation in decades because there was no need for that. We’re going to find that the kind of safeguards we have for moving the volumes of oil we are, are woefully inadequate.

Baillieul: Are the regulators asleep at the wheel?

Jeff Rubin: Well, maybe that’s a little unfair. Maybe you could say they were asleep at the wheel of a car that wasn’t moving.

Because rail hasn’t played this role in the oil industry since the days of the Rockefellers. You have to go back to the beginnings of the oil industry in North America. So maybe it's understandable why we haven't overhauled our rail safety standard. But the world has changed almost overnight.

I'm saying our rail regulations haven't really been looked at for decades. Maybe understandably so, because there was no reason to. But there is certainly reason now.

Baillieul: Dose a regulatory clampdown represent a major threat to the rail industry?

Rubin: Threat? What's it's going to do, starting off with the kind of rail cars that are being used, it's going to add to the cost of rail transit. It already costs about $10 per barrel to move oil from the Bakken in North Dakota to a refinery on the east coast. We might even see those costs double or triple as all of a sudden the regulatory environment changes and, for example, we have to order a whole new stock of roiling trucks to move oil. So what I think we're going to find is that the cost of rail transit are going to rise.

It's no different than in nuclear. When there's an accident in nuclear the tendency has been — and this is true of Three Mile Island and Chernobyl and it will probably be true of Fukushima — the cost of building new nuclear plants went up 90%. All of a sudden there were additional safeguards and requirements that came into play that didn't exist before.

I'm not saying 90%, but I think we can see a significant increase in the cost of rail transit as we tighten up the safety requirements.

And that goes back to my original point — the Achilles' heel of North American energy independence, whether it's trying to double oil sand production in Alberta or double shale oil production in the Bakken, is that we don't have the infrastructure to move that increased production.

Baillieul: Thanks for taking the time to speak with me, Jeff. Just circling back to your book *The End of Growth*, is there anything you'd like to tell our readers or anything that keeps you up at night?

Rubin: Yeah, I'll tell you what I find pretty bizarre. Maybe this is why David Suzuki has endorsed the revised paperback version of my book because he's the only guy who thinks what I have to say is bullish. But buried beneath the headlines of the fracking revolution or the United States to produce more than Saudi Arabia blah blah blah, was the finding by this laboratory in Hawaii that we've already hit 400 parts per carbon.

We're looking at all these so called increase in hydrocarbons and totally oblivious to what would happen if we combust all of this stuff. And even the International Energy Agency — which is hardly the Suzuki Foundation or the WWF [World Wildlife Fund] — gave us less than a 20% chance of avoiding a four-degree rise in global temperatures over the next five or six decades. So it certainly casts a different perspective on this abundance of hydrocarbon resources that the industry claims it has found.

The good news story is, ironically, that no matter where you look, economies aren't growing like they used to and nowhere is that more evident than in China. Last year, China combusted 4 billion tonnes of thermal coal. Maybe China won't be combusting 4 billion tonnes of coal in the future if the economy is growing at a 5% rate rather than a 10% rate.

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Disclosure: Robert Baillieul has no positions in any of the stocks mentioned in this article. Fool co-founder David Gardner owns shares of Canadian National Railway.

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