What are the Biggest Threats to Cenovus' Future?

Description

Cenovus Energy (TSX: CVE) (NYSE: CVE) is sitting on a pile of oil. Because of this the opportunity before the company is pretty remarkable. That said, Cenovus faces several threats that it must overcome in order to fulfill its potential as a great Canadian oil growth company. Let's take a closer look at the two biggest threats facing the company.

Environmental issues with the oil sands

One of the biggest threats to the future development of the oil sands is its environmental impact. The bitumen that is produced emits more greenhouse gasses than conventional oil production. Not only that, but oil sands mining operations disrupt the land. Finally, if diluted bitumen were to spill from a pipeline incident, it's harder to clean up than traditional oil.

Because of these environmental shortfalls, the industry is under intense pressure from environmental groups. While that pressure does force change within the industry, there is a risk that overly burdensome regulations could cause oil production to be curtailed. That would impede companies like Cenovus from fulfilling the potential to deliver outstanding long-term returns for investors.

Processing problems

The environmental issues surrounding the oil sands is causing a delay in critical pipeline infrastructure such as the Keystone XL pipeline by **TransCanada**. This is forcing producers like Cenovus to endure lower prices for the oil that is sold because it's taking longer for the oil to reach refineries and in some cases it needs to be transported by more expensive railway options.

The other issue is that not all refineries can handle heavy Canadian crude oil. This is where Cenovus' integrated approach should help it in the future. The company jointly owns the Borger and Wood River Refineries in the U.S. with refining giant **Phillips 66** (NYSE:PSX). Both refineries can refine Canadian crude oil, however, debottlenecking at the Wood River facility could increase its heavy oil processing capacity by 10%.

Its relationship to refining giant Phillips 66 could prove to be very beneficial in the future as Phillips 66 is investing heavily to increase its ability to process cheaper crude oil. At the same time, if Canadian crude gets too expensive due to environmental regulation or continued pipeline issue it could force Phillips 66 and other refiners to look elsewhere for oil.

Investor takeaway

Processing problems at other refiners or pipeline bottlenecks could impact Cenovus' ability to produce enough profit to earn sufficient returns for investors. Further, Phillips 66 and Cenovus could be forced to spend heavily at the jointly owned refineries to satisfy tougher future environmental regulations. Finally, if the TransCanada's Keystone XL is not built in the future it could severely impact the availability of future pipeline capacity to get oil out of Canada, also impacting Cevovus' margins.

While these are two major threats, neither seems impossible to overcome. America needs Canada's oil. The industry will do what it takes to profitably get that oil out of Canada and into the hands of American consumers. That should enable Cenovus to earn its investors a very nice long-term return.

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