



The Oil Sands Crisis Nobody Is Talking About

Description

Yesterday evening, French energy giant **Total** told investors that it would be shuttering its upcoming oil sands project.

The project, dubbed Joslyn, is a joint venture between Total and a number of different oil companies. The most notable partner for Canadian investors is **Suncor** ([TSX: SU](#))([NYSE: SU](#)), which owns 36.75% of the failed project. This was just barely less than Total's 38.25% interest.

The head of Total's Canadian division had this to say about why the company is pulling the plug on the project: "Joslyn is facing the same challenge most of the industry world-wide [is], in the sense that costs are continuing to inflate when the oil price and specifically the netbacks for the oil sands are remaining stable at best — squeezing the margins."

Joslyn has been plagued with problems from the start. Originally, Total planned to use wells instead of trucks and shovels to extract the bitumen. This quite literally blew up in its face when one of the company's wells exploded.

This isn't the first time a joint venture between Suncor and Total has ended up badly. In 2013, both companies decided to call it quits on an upgrader project in the same area called Fort Hills. Suncor's management hasn't quite closed the book on either of these failed projects, stating it will likely revisit each in a few years.

Of course, Suncor is still a dominant oil sands player. The company's most recent results showed production of more than 400,000 barrels of oil per day just from the oil sands, a record high. Suncor is by far the largest producer in the region, easily outpacing other producers like **Canadian Oil Sands** ([TSX: COS](#)), **Canadian Natural Resources** ([TSX: CNQ](#))([NYSE: CNQ](#)), and **Imperial Oil** ([TSX: IMO](#))([NYSEMKT: IMO](#)).

The bigger issue

This news is important to investors for one main reason: It symbolizes how much of a problem cost overruns are for oil sands producers.

I'm from rural Alberta. I know many people who have spent time working up in the oil sands. At first, most are gung-ho. There's a certain excitement about working so far away from home, and their employers ensure everything is taken care of. Huge camps not only house the workers, but also feed them and keep them entertained.

And, of course, there's the money. Oil sands workers are paid two to three times what regular workers are paid for the same job. It's not uncommon to see ambitious workers make more than \$200,000 per year *after* tax. There are stories about people heading up to the oil sands as 22-year-old fresh graduates and coming back five years later as millionaires.

And yet, even after all those efforts, oil sands producers are still having problems attracting staff. Many workers go in for a few months at a time and then leave, unable to handle any additional time away from their families. Boredom is a common problem in the camps, and both drug and alcohol use are common.

Oil sands producers are stuck in a tough spot. They need to get employees up to northern Alberta, and are willing to offer a huge premium to do so. Once you factor in other fringe benefits received by staff, this becomes an almost prohibitive cost, especially for producers that have already paid a premium just to be in the region.

During the early days of the oil sands, this wasn't such a big deal. It was so cheap to produce that increased costs were just a minor inconvenience. These days, that easy oil is mostly a thing of the past. New projects have much higher costs than previous generations, and that's not even including staff.

Production in the oil sands used to be a slam dunk. Now, cost overruns are a major issue. Investors need to be aware of this, and realize that any sustained drop in oil prices could majorly curtail oil sands production. The days of oil sands operations being low-cost are largely over. Look for more of these projects to be suspended in the future.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:CNQ (Canadian Natural Resources)
2. NYSE:SU (Suncor Energy Inc.)
3. TSX:CNQ (Canadian Natural Resources Limited)
4. TSX:IMO (Imperial Oil Limited)
5. TSX:SU (Suncor Energy Inc.)

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