



Oil Prices Could Soon Become a Major Long-Term Problem for Canada

Description

One of the top energy intelligence firms, Wood Mackenzie, has some bad news for Canada's oil sands industry. If current low oil prices persist, then as many as 16 oil sands project phases could be at risk of being deferred. This would really slow down future growth as the long lead time of these projects means that investments not made today will impact production a few years down the road. That said, analysts do see some opportunities on the horizon that investors should keep an eye on.

Putting the brakes on investment

Analysts at Wood Mackenzie are now estimating that oil producers will firmly apply the brakes to capital spending on new oil sands project phases. This could lead to [upwards of \\$60 billion in investments](#) not being sanctioned over the next three years. If that happens, it would set the stage for a big drop off in production growth for companies toward the end of the decade.

We're already seeing evidence of this at **Suncor Energy Inc** ([TSX:SU](#))([NYSE:SU](#)), which [recently announced](#) that it was cutting a billion dollars from its capex plan. While the company will continue to invest in its Fort Hills project, it is deferring spending on MacKay River 2, which is a project it had yet to sanction for development. We're seeing a similar slowdown on longer-term strategic spending at **Cenovus Energy Inc** ([TSX:CVE](#))([NYSE:CVE](#)). In late 2014, Cenovus Energy put out its capital budget for 2015, which included big reduction in spending on emerging oil sands assets as it's deferring some investments until the company has more clarity on oil prices.

That said, because of the extremely long time it takes to build oil sands assets, these deferrals won't impact oil sands producers for several years. This is because currently sanctioned projects at many companies have basically locked in production growth through 2017. These recent deferrals, however, will have an impact on production growth beginning in 2018, which means that the oil price collapse over the past few months could have a long-term impact on the industry that could be felt long after prices correct.

Turing to acquisitions for growth

The other long-term impact from the current turmoil in the oil market is that it should open up the doors

for deal-making to return to the oil sands according to Wood Mackenzie. The industry has been “markedly quiet over the past two years” according to Wood Mackenzie, but that should change as the low oil price environment could force producers to consolidate operations to keep costs low. It could also attract foreign buyers as Canada might be open again to outside capital in order to keep the industry from stagnating due to low oil prices.

Big North American oil giants like **Chevron Corporation** ([NYSE:CVX](#)), for example, could decide to take advantage for the current turmoil to bolster its presence in the oil sands. The company’s only exposure right now is a 20% interest in the Athabasca Oil Sands Project. However, it has the access to capital and the long-term outlook needed to make a move in this environment. Likewise, foreign buyers could begin to look for opportunities in the oil sands now that the region will likely need outside capital now that its own oil cash flows will be coming down.

Investor takeaway

The significant drop in oil prices is starting to have an impact on the long-term growth of the oil sands. We’re seeing producers put the brakes on spending for new projects, which will likely impact production growth in 2018 and beyond. Further, there could be a big shake-up in the industry as it’s a prime target for merger activity. While this means that a turnaround could be very slow to develop, the upside from a buyout could buoy oil sands stocks.

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