The 5 Biggest Risks Facing Canadian Energy Investors

Description

Canada has vast energy resources. It has the third-largest proved oil reserves in the world and is the world's fifth-largest natural gas producer. The country's abundant resources could make Canada an energy superpower. However, the country could face five major risks that could prevent these resources from creating wealth for Canada and those investing in Canadian energy stocks.

Risk No. 1: Oil prices

Canada's vast oil resources aren't cheap to develop, and most sources require massive capital spending to get the oil out of the ground. Because of that, the recent deep drop in oil prices has put future development on hold.

Suncor Energy Inc. (TSX:SU)(NYSE:SU) recently cut a billion dollars from its capex program and deferred its MacKay River 2 oil sands project and its White Rose Extension offshore project. These projects, which were expected to begin producing in 2017 might not produce oil for years if prices remain weak.

Meanwhile, low oil prices forced **Canadian Natural Resources Ltd.** (TSX:CNQ)(NYSE:CNQ) to cut its capital budget by 28% to $6.2 billion with the Kirby North Phase 1 project being the biggest casualty of that cut. The list goes on and could get longer if oil prices remain weak for a few years.

Risk No. 2: Not in my back yard

Even before the recent drop in oil prices, Canadian oil producers were realizing much less for their oil than others around the globe because the country doesn't have enough pipeline capacity to get oil out of the oil sands region and into market centres.

There are a number of major oil export pipelines that have been proposed to fix this problem, including **Enbridge Inc.'s** North Gateway, **Kinder Morgan Inc.'s** Trans Mountain expansion, and **TransCanada Corporation's** Keystone XL and Energy East projects.

However, each project faces major opposition from environmentalists and locals who don't want to see an oil sands pipeline built in their backyard. This opposition has delayed some projects for years and makes one wonder if there will ever be another oil sands export pipeline built, as all major routes seem blocked by opposition.

Risk No. 3: Growth derailed

Because there's not enough pipeline capacity, railway companies like **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) and **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) have helped to fill the gap by shipping crude by rail. However, the increased shipments of crude have led to a worrisome uptick in train derailments.

In fact, according to a recent report, train derailments at Canadian National are up 73% from the prior year, though derailments at Canadian Pacific are on par with prior years. Still, the overall increase in derailments, especially those involving crude, could put the brakes on the growth of this mode of transportation and leave Canadian oil producers with limited options for moving oil.

Risk No. 4: Environmental costs

One reason why there has been such intense opposition to new oil sands pipelines is because oil is seen as being more carbon intense than conventionally produced oil. This is due in part to the fact that a lot of natural gas and diesel is consumed to get the oil out of the ground.

Oil sands production alone accounts for 7.8% of Canada's greenhouse gas emissions and 0.1% of total global emissions and the high range of life-cycle emissions are higher than all other sources of crude in the world.

This is why environmentalists are pushing back against pipelines and new oil sands developments, which is adding to the costs of oil sands projects as companies need to invest to reduce their carbon footprint. These investments impact current returns and future growth.

Risk No. 5: Business climate

Canada has enough natural gas potential to become a leading LNG exporter in the years ahead. However, it's becoming less likely that the country will ever reach its potential. **Royal Dutch Shell** (NYSE:RDS-A)(NYSE:RDS-B) believes only 15-20% of currently approved projects will be developed over the next decade. This is due to a combination of factors, including cost, lack of skilled workers needed to build these projects, complicated tax and regulatory environments, and local opposition.

Investor takeaway

Canada is blessed with abundant energy resources. However, it faces enormous risks in getting that energy out of the ground and into world markets. This is keeping a lid on the country's ability to turn its resources into wealth.

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