How Bad Is Canada's Oil Bust? Try the Worst Spending Drop in 70 Years

Description

We all know that the oil bust has hit Canadian oil producers pretty hard. They've slashed or suspended dividends, reduced the headcount, shut down uneconomic wells, and have significantly reduced capex spending. In fact, they've now cut back capex spending to such a degree that it marks the largest two-year decline in the past 70 years.

It could be even worse

Overall, oil and gas producers in Canada have cut a whopping $50 billion in capital investments over the past two years. That's the biggest two-year decline since at least 1947, which is when the Canadian Association of Petroleum Producers started tracking investment spending.

In percentage terms, producers have now cut spending by 62% since it peaked at $81 billion in 2014, with spending in the oil sands being cut in half to just $17 billion. That's the lowest investment rate for the region since just after the financial crisis.

However, spending in the oil sands region would likely be even lower if it wasn't for the long lead time of these projects; the bulk of 2016's investment dollars are being spent on projects that started construction prior to the downturn.

For example, **Canadian Natural Resources Limited** (TSX:CNQ)(NYSE: CNQ) is still working on phases 2B and 3 of its Horizon oil sands project. That expansion accounts for roughly $2 billion of its planned $3.5-3.9 billion of capital spending this year, which is down 22% from what it had projected to spend this year.

Suncor Energy Inc. (TSX:SU)(NYSE:SU), likewise, is still funding the investment to build its Fort Hills oil sands mine, which won't deliver first oil until next year. In addition to that, it's also investing in the Hebron offshore platform, which also won't produce a drop of oil until next year.

Focusing on survival

Large producers like Suncor Energy and Canadian Natural Resources are still investing in these massive projects because they have the capital to do so. Suncor Energy, for example, is sitting on over $4 billion in cash, which is enough to fund the bulk of its growth spending. Meanwhile, Canadian Natural Resources expects that it will be cash flow positive once Phase 2B starts producing later this year, which is why it continues to pour money into that project.

The same, however, can't be said about smaller producers like **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE) or **Pengrowth Energy Corp.** (TSX:PGF)(NYSE:PGH), both of which cut investments substantially; for example, Penn West cut its spending by 90% last year. These smaller producers have been much more deeply impacted by the downturn because of their weaker balance sheets and asset base.

In fact, Penn West estimates that if oil remains weak, it could default on its debt covenants as soon as the end of the current quarter, while Pengrowth Energy could do the same by the end of the year if oil spends too much of the year below $30 a barrel.

Meanwhile, the oil price is so weak right now that Penn West has had to shut down 4,000 BOE/d of uneconomic production; it expects another 2,500 BOE/d of production to be shut down because it doesn't have the funds to make repair projects on the equipment needed to keep these wells pumping. Likewise, Pengrowth has had to shut down 930 BOE/d of uneconomic production.

Investor takeaway

The numbers are in and this is officially the worst oil bust to hit Canada in at least the past 70 years. The downturn actually could have been a lot worse if it wasn't for the fact that larger producers had the capital to keep investing in projects that had been started before oil prices turned south.

As such, the worst might not be over because these producers will likely cut spending even more next year, while smaller players could go bust if oil doesn't meaningfully recover by the end of this year.

CATEGORY

1. Energy Stocks
2. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

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

Category

1. Energy Stocks
2. Investing

Tags

1. Editor's Choice

Date
2025/08/29
Date Created
2016/04/13
Author
mdilallo