



Despite Getting the Green Light, These Oil Sands Projects Might Never Move Forward

Description

Last week the government in Alberta approved three oil sands projects. These were the first project approvals under the government's Climate Leadership Plan, which put a cap on greenhouse gas emissions. That said, despite getting the green light from the government to move forward, none of the producers are ready to make a final investment decision to start construction. Given the current oil market, it is entirely possible that producers will never move forward with these projects.

The \$4 billion question mark

The projects to win approval are the Blackrod and Wildwood projects from private producers Blackpearl Resources and Surmont Energy, respectively, and **Husky Energy Inc.'s** (TSX:HSE) Saleski project. Combined, these projects are designed to produce 95,000 barrels per day and, according to estimates, it would cost roughly \$4 billion to construct all three projects.

That hefty price tag alone could cause these projects to remain on the to-do list for quite some time because producers no longer have open access to capital to fund the upfront investment.

For example, when Surmont Energy started the process on Wildwood in October 2012, it had interest from several financial backers for the US\$375 million, 12,000-barrel-a-day project. However, at that time crude was around \$90 a barrel, which is double where it is today. That lower oil price could make it much harder for the private company to get the financing it needs to move forward with the project, assuming it is even economic in the current environment.

Unappealing economics

The questionable economics are another major factor that could keep these projects on the drawing board for quite some time. For example, while Husky Energy said it would review moving forward with Saleski "in light of our current budgeting process," the projected returns from the project suggest that the review will not take long.

According to an investor presentation from the company, Saleski requires oil prices north of \$80 a

barrel just to deliver a nominal 10% internal rate of return. Because of that, it would be impossible for the company to justify an investment in the project in the current environment.

Further, it has several other future projects that can easily meet that 10%-return hurdle at current oil prices with additional projects that meet it once oil is in the \$50-60 a barrel range. Because so many other projects have better economics than Saleski, Husky Energy will likely move forward with those projects first and only consider it if oil prices re-approach to their 2012 level.

Investor takeaway

While it is nice to see that oil projects can win approval under the new Climate Leadership Plan, they still need to make economic sense before producers sanction the projects. Given the current environment, that will be the harder sell because not only is capital tight, but the economic returns don't appear to be there given current prices. So, unless prices vastly improve, these projects will likely remain on hold for quite some time.

CATEGORY

1. Energy Stocks
2. Investing

POST TAG

1. Editor's Choice

Category

1. Energy Stocks
2. Investing

Tags

1. Editor's Choice

Date

2025/08/18

Date Created

2016/09/21

Author

mdilallo

default watermark

default watermark