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POTEN TANKER OPINION

The End Of The Line(s)

The Keystone XL Pipeline is cancelled (again)

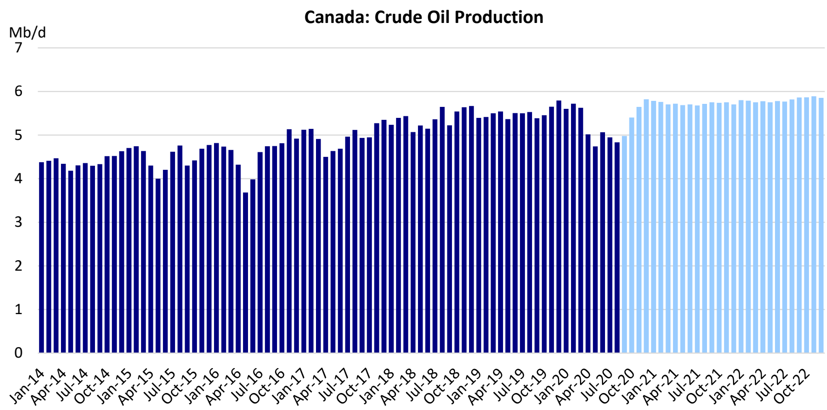
One of the first executive actions of President Biden was to block the Keystone XL pipeline by withdrawing the permit for the project. While this move was expected, it was loudly criticized by Canada's oil producers and the government of Alberta. Billions of dollars have already been invested in the project and stopping it will lead to significant jobs losses. Keystone XL is not the only Canadian pipeline that is at risk. Several other cross-border pipelines have been under attack as well and further setbacks could limit Canada's crude oil export potential. Canada is building other pipelines and companies are considering alternatives, but oil pipelines continue to face strong opposition. What will the implications be for Canadian production and exports?

In November 2020, the governor of Michigan ordered Canada's Enbridge to decommission Line 5, a 645-mile pipeline that runs from Superior, Wisconsin to Sarnia, Canada. It transports about 540,000 b/d of light crude oil and natural gas liquids to refiners in Michigan. Enbridge has resisted closing the pipeline, claiming that the pipeline is safe. Enbridge is also facing pushback on another cross-border pipeline: Line 3. After years of environmental reviews and permitting, construction had started on the Minnesota portion of Enbridge's new Line 3. The project will replace the old Line 3, which was built in the 1960s and runs 1,097 miles from Edmonton, Alberta to Superior, Wisconsin. Upon completion, the initial annual capacity of Line 3 will be 760,000 b/d.

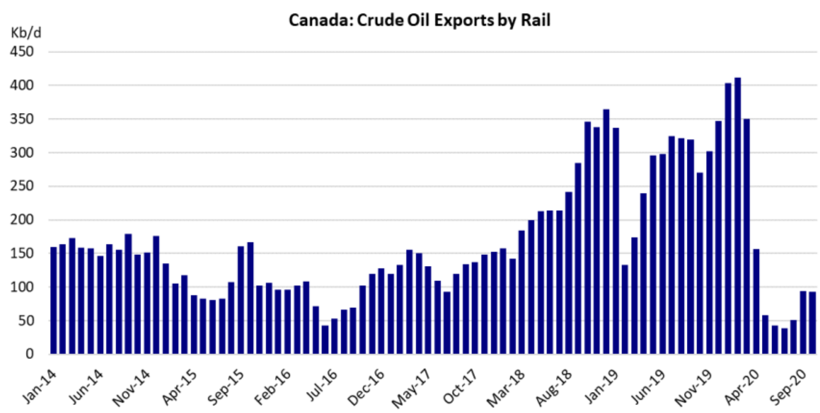
Restricting cross-border pipelines from Canada to the U.S. will pose more challenges for Canadian producers than for U.S. refiners. As a result of the shale boom, the U.S. is awash in domestic crude oil and there is little or no need for additional supplies from Canada at the moment.

Canadian producers, on the other hand, will be facing growing challenges bringing their crude oil to market. Canadian oil production, 90% of which comes from Western Canada (Alberta, Saskatchewan, Manitoba and British Columbia), reached 5.8 Mb/d in December 2019. Production declines and transportation restrictions resulting from Covid-19, temporarily reduced output to below 5 Mb/d. However, the EIA estimates that Canadian production did already recover to pre-Covid levels by the end of 2020 and is expected to exceed 2019 levels in 2022 (Chart 1). Some analysts and company executives expect even more expansion. Enbridge forecasts an additional 1.0 Mb/d through the 2020s. On that basis, significant additional takeaway capacity is needed.

Even if no new capacity can be added, some of the existing pipeline networks can be expanded by adding pumps and/or using more drag-reducing agents. Another tried and tested method of moving oil over long distances is by rail, and both Canadian producers and the North American rail conglomerates are highly experienced users of crude by rail. Although it is more expensive that pipelines, it offers flexibility and provides significant spare transportation capacity. As Chart 2 shows, Canada exported more than 400,000 b/d of crude oil by rail in the early months of 2020. This capacity is still available and can be brought back online fairly quickly.



Source: EIA



Source: Canada Energy Regulator

The policies of the Biden administration towards the fossil fuel industry and their focus on addressing climate change means that most of the additional production out of Canada will be headed for the export markets outside of the U.S. Asian markets, in particular China, can be reached via shipments through the Trans Mountain pipeline (expanded to 890,000 b/d when finished by the end of 2022). Another outlet for Canadian crude would be the U.S. Gulf. Plans to reverse the flow of the Capline pipeline will give Canadian crude greater access to refiners and export terminals along the Gulf Coast. Initial capacity will be 300,000 b/d. Exports from there could also target Asia (on VLCCs) and/or Europe (on Aframaxes/Suezmaxes). Chances are that the tanker industry will benefit from more Canadian crude, one way or another.

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