Costs of Canadian Oil Sands Projects Fell Dramatically in Recent Years; But Pipeline Constraints and other Factors Will Moderate Future Production Growth, IHS Markit Analysis Says

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WASHINGTON--(BUSINESS WIRE)--The cost of building and operating oil sands projects has fallen dramatically in recent years and total oil production is expected to rise by another 1 million barrels per day (mbd) by 2030. But external factors—such as price uncertainty caused by pipeline constraints—are contributing to a more moderate pace of production growth than in years past, a new report by business information provider IHS Markit (Nasdaq: INFO).

The report, entitled Four Years of Change, examines oil sands cost and competitiveness in the years following previous IHS Markit research on the topic. The report and previous oil sands research is available at www.ihsmarkit.com/oilsandsdialogue.

The cost to construct a new oil sands project is anywhere between 25 percent and a full one-third cheaper than in 2014, the report says. Deflation in capital costs was a factor. But reengineering—efforts such as simplifying project designs, building for less, and more quickly constructing and ramping up production—has also played a major role in the reductions.

The costs associated with the operation of oil sands projects have fallen even more dramatically. Operating costs for both oil sands mining operations with an upgrader and steam-assisted gravity drainage (SAGD) facilities fell by more than 40 percent on average from 2014 to 2018. Increased reliability—reducing facility downtime and increasing throughput—was the biggest factor in the cost savings, which went as high as 50 percent in some cases.

"It is important to note that the largest share of these cost savings are coming from structural changes, the way projects are designed, constructed or operated," said Kevin Birn, vice president, IHS Markit – who heads the Oil Sands Dialogue. "These types of savings tend to be more permanent. This means that oil sands costs have a greater potential to remain in check should inflationary pressures resume."

These cost improvements have lowered the breakeven oil price for new oil sands projects—the price of oil required for a project to cover and earn a return on investment, the report finds. IHS Markit estimated that the lowest-cost oil sands project (expansion of an existing SAGD facility) required a more than $65 per barrel price for West Texas Intermediate (WTI) crude to break even in 2014. Today, the breakeven price has fallen to the mid-$40 per barrel range. Likewise, an oil sands mining project without an upgrader required a near-$100 per barrel breakeven price in 2014 compared to around $65 per barrel in 2018.

Despite these sizeable cost reductions, the western Canadian oil market continues to move through a period of price uncertainty due to significant delays for advancing pipeline projects, the report says. The lack of transport capacity forced many producers to take deep discounts for their barrels late in 2018.

In 2018 the western Canadian heavy oil differential averaged $27 per barrel below the WTI price—more than double what it was in 2017. Over the course of a year the differential fluctuated wildly from $11 per barrel to more than $50 per barrel beneath WTI—the worst level in recorded history. Since then the Alberta government has imposed an oil production cap and differentials have generally trended in a narrower range. However, should Alberta continue a process of loosening the production limits in the coming year the differentials are likely to widen again, the report says.

Growth in the Canadian oil sands will continue, albeit at a slower pace, the report says. IHS Markit expects over the coming decade year-on-year oil sands production additions will average beneath 100,000 barrels per day (b/d) per year—down from average annual rate of 160,000 b/d or more during 2009-2018. The reduced production outlook will nevertheless be sufficient for oil sands to top 4 mbd by 2030, a million barrel per day increase from 2018.

“Oil sands economics have improved dramatically over a very short period,” Birn said. “Still ongoing constraints continue to weigh on timing of future investments and the investment and the growth outlook continues to moderate. But growth is still anticipated.”

“Nearly one-third of growth in the IHS Markit outlook to 2030 comes simply from the ramp up, optimization and then sustaining of existing facilities. There is upside potential, but the key will be the ability of government and industry to restore confidence that Canadian crude will get to market, whether by pipe or rail.”

Four Years of Change and all other Oil Sands Dialogue research is available to download at www.ihsmarkit.com/oilsandsdialogue.
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