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Silent boom takes root in oil sands: From retreat to rebound in one year

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CHRISTINA LAKE, ALTA. -- Tucked next to the web of steel and pipe that wrings thick bitumen from this corner of northeastern Alberta, a pile-driving machine slams a long steel pipe into the soft earth that covers the province's oil sands.

When it is deep enough, the pipe will help support a massive expansion of the extraction facility at Christina Lake, a Cenovus Energy Inc. project that currently produces 15,500 barrels per day. By 2019, the company says the facility will be capable of churning out some 258,000 barrels daily, a massive 17-fold increase.

The deep pulsating beat of the pile-driving machine is the sound of a resurgence in Canada's oil sands industry. Only a year ago, the sector was in retreat, battered by a global economic crisis that sank oil prices and forced energy companies to slash production, shelve planned projects and cut spending.

Yet in the span of a few quarters, the oil sands have managed an impressive reversal. The rebound has been gradual and grabbed few headlines as companies take a measured, deliberate approach to expansions. But a silent boom has spread across the energy industry, creating both new flickers of confidence - and a surprisingly loud echo of the problems that previously weighed on company finances and crippled some firms with oil production plans that proved too ambitious.

The cost of building a new oil sands project now exceeds the levels seen at the heights of 2008, when oil hit $147 (U.S.) a barrel and Fort McMurray was at the centre of a raging inflation wildfire.

Suppliers that were offering 10- to 40-per-cent discounts last year have almost entirely clawed back those reductions. The number of workers in oil sands camps has topped the peak in 2008.

After a year of quieter highways, the traffic jams are back in Fort McMurray, and home prices in the oil sands headquarters are back within spitting distance of their apex.

The current surge is founded in part on the remnants of the last boom. The thousands of workers building Royal Dutch Shell PLC's Jackpine River mine, for example, have yet to finish that project, but soon will.

But new anchors are also emerging. Imperial Oil Ltd., and its new $8-billion (Canadian) Kearl mine, is the most obvious example. A remarkable array of smaller work has also been put in play. Companies such as Statoil, MEG Energy Corp., Connacher Oil and Gas Ltd., Devon

Energy Corp., ConocoPhillips, Athabasca Oil Sands Corp., Suncor Energy Inc. and, of course, Cenovus, are each building new capacity.

Rather than the six-figure increases of the past - Shell's Jackpine, for example, is adding 100,000 barrels per day of capacity - these new projects are building more slowly, adding tens of thousands of barrels. The smaller size of the new projects is one reason for the lower profile of this boom.

Add up the recent developments, however, and it is clear that the dark days of 2009 are now in the past. The Canadian Energy Research Institute calculates that in late 2008 and 2009, companies paused or abandoned a million barrels per day of production. Since then, they have brought back to life 1.4 million barrels a day - a substantial increase.

As workers return to northeastern Alberta, so is the belief that the bad times are over.

"It won't be slowing down here for quite a while," says Leonard Wourms, a power engineer and shift co-ordinator at Christina Lake. He stands next to shining lengths of silver pipeline that snake out from the Cenovus extraction facility to the cleared fields where wells are now being sunk into the bitumen.

A year ago, the pipe didn't exist. By next year, the bitumen will be flowing.

"They'll just keep going, expanding from here," he says.

OUT OF THE RECESSION

Before last year, Michael Morin had never experienced a recession. In January, 2003, when the last boom was beginning to gather steam, the Fort McMurray helicopter pilot formed Wood Buffalo Helicopters. He started with just one machine.

The company was immediately profitable and, from 2003 to 2008, its fleet grew from one helicopter to eight. Then 2009 hit and, with the fall in oil sands activity, came Wood Buffalo's first tumble. Revenue dropped 40 per cent. Mr. Morin cancelled an order for a new helicopter.

Now, work is beginning to return. After a slow first quarter, "the oil sands companies gave the green light to some project work in the second and third quarters," Mr. Morin said.

Costs had, after all, fallen. Contractors desperate for work were slashing prices. Eyeing an opportunity, some energy companies leapt back to work.

"The contractors all came to the table with price rollbacks," said Ab Beisel, drilling co-ordinator for Cenovus at Christina Lake. "We basically took advantage of that, and the availability of the extra labour pool, and kept the people working."

One of the best ways to see the impact of those decisions is from the window of one of Mr. Morin's helicopters, looking down on the oil sands camps that accommodate trade and construction workers. According to the Oil Sands Developers Group, an industry association that tracks the numbers of commuting workers, those camps are now more full than they've ever been, with 3 per cent more workers than in 2008.

With the return of workers has come a new round of frenzied home-buying in the city at the heart of it all - a sure indication that the good times are back. Colin Hartigan, president of Fort McMurray Realtors, says prices peaked in July, 2008, when the average cost of a single-family home rose to $697,970. This July, house prices hit $689,700, just 1 per cent from the peak.

"We've seen a jump back to what we were witnessing two or three years ago," said Guy Boutilier, a local MLA with the opposition Wildrose Alliance Party of Alberta. "It's bordering on the edges of insanity. I don't know how else I can best describe it."

RISING COSTS A CONCERN

Those close to the recovery caution that it may be frail. If oil prices fall again, work could once more be halted.

This boom is substantially different from the last one, when costs were rising by double-digits every year. Executives say inflation today is nearer five per cent a year.

Still, the cost of new projects has already surged beyond its 2008 peak. Recent filings from MEG Energy and Athabasca Oil Sands show construction prices have risen to between $34,000 and $38,000 per flowing barrel, a key industry metric, beating the $32,000 seen in 2008.

These are "levels not seen before, except for marginal plays," said Peter Howard, interim president of the Canadian Energy Research Institute. "The resurgence in oil sands planning is bringing about a dramatic rise in costs."

In fact, inflation has again become a concern across the industry. Royal Dutch Shell, for example, has scaled back plans for an area it says is too expensive. Chris Seasons, president of Devon's Canadian operations and chair of the Canadian Association of Petroleum Producers, said that while some equipment costs remain lower than before, overall costs on coming projects will likely exceed those on past ones. "We're counting on increases in labour costs over a couple of years ago," he said.

But he added: "Although we're seeing some pressures, it doesn't feel at all like 2008 to me. I haven't heard any of my peers complaining bitterly about the challenges, in terms of both acquiring labour, getting skilled labour and also the cost of that."

Indeed, projections of future needs for workers have eased. Last year, the Alberta government trimmed its projected worker shortfall by 17 per cent, to 77,000, over the next decade. That remains, however, a substantial shortage - and near Fort McMurray, worry is beginning to surface that problems are once again imminent.

Take Christina Lake, where only one drill is turning this summer. By winter, when the muskeg is frozen and work can proceed more easily, the number will increase to as many as 10. That has Mr. Beisel, the drilling co-ordinator, wondering how he will find enough people to keep the oil sands booming. "There's going to be major shortages," Mr. Beisel said. "It's going to be bad."

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Signs of resurgence

27,715

Number of workers in oil sands camps, 3 per cent more than at 2008 peak.

$689,700

Average house price in Fort McMurray, 1 per cent below 2008 peak.

$34,000 to $38,000

Construction prices per flowing barrel, beating the $32,000 seen in 2008.