

# Iraq developments underline strategic value of Canadian oil sands

If ever there was a doubt that the output of Canada's oil sands needs to be increased, the Islamic State of Iraq and the Levant (ISIL) have removed that doubt. Once again, we have been reminded by the insurgent takeover of parts of western Iraq that Middle East oil is vital but potentially the subject of political instability and security challenges. And it will be again a decade hence when crude output in the United States begins to plateau by the mid-2020s. As the International Energy Agency (IEA) has stated, by that time it will be the Middle East again that will provide the necessary sources to meet oil demand. In a recent interview IEA executive director Maria van der Hoeven made the point that "the Middle East's increased investments remain absolutely critical to the long term outlook for oil markets".

In fact, according to a report this week in Canada's *Financial Post* the IEA believes that country's oil sands industry needs to invest \$42 billion a year through 2035 to ensure the industry remains an engine of growth (and an alternative to the Middle East). It will be needed, not only for Canada and the U.S. but also energy-hungry Asia. Reports this week also quote a senior executive of India's ONGC (Oil and Natural Gas Co) saying pipelines have to be built to transport the oil before it will invest in oil sands production.

In view of what has happened in Iraq in the past few days, we have had a sharp reminder of how important are longer-term investment in alternatives to Middle East oil.

"Iraq oil infrastructure at risk" is a report out today from Deutsche Bank. It says the outbreak of violence by ISIL Sunni

rebels has introduced a new event risk for global oil markets. Iraq has the fifth largest oil reserves in the world and has now passed Iran to become the second largest producer in OPEC. The Sunni activity has so far been confined to the north of the country so it is not yet posing a risk to most of Iraq's oil output. Deutsche says the more immediate problem is the threat to Iraq's refining capacity: the insurgents are active in Mosul province and the country's largest refinery, Baiji which processes 310,000 barrels a day, is located near Mosul. But this may not be the extent of the uprising. "The speed of the ISIL progress and its fortification with newly acquired weaponry suggests that this may be more than a temporary incursion," says Deutsche.

If ISIL is able to make southward progress towards Baghdad this will heighten instability in the country and possibly threaten the smooth operation of existing refineries and oil fields. The bank says the greatest concern would be any detrimental impact on investment in new capacity. Now producing about 3.4 million barrels a day, the world is depending on Iraq expanding to 4 million barrels a day by the end of this year and then heading to 5 million barrels.

As Deutsche points out, this comes against a background where production in recovery in Libya has been much slower than expected.

But, even if ISIL does not manage to disrupt much of Iraq's oil output, it still throws a large question mark over reliability of the Middle East. There always seems to be a new drama breaking out somewhere in that region.

Yet here we have the Canadian oil sands with their estimated 168 billion barrels of oil, a resource of black gold exceeded by only those of Saudi Arabia and Venezuela. In 2012, oil sands output reached 1.8 billion barrels a day, so the industry has become a meaningful player in the oil business.

Next week the federal government in Ottawa is expected to make a decision on Northern Gateway, the pipeline intended to deliver crude from the oil sands of Alberta to the British Columbia coast for export.

The events now under way in Iraq underline the future importance of this energy source.