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ENERGY SECTOR

Financier Worldwide canvasses the opinions of leading professionals around the world on the latest trends in the energy sector.

CANADA

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Respondent

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Q. Reflecting on the last year or so, what major trends would you highlight in the energy sector in Canada?

A. There are a number of significant trends in the energy sector in Canada that could be highlighted, but three stand out. The first is the industry's financial and commercial support for the cleantech sector. The oil & gas sector is the largest investor in Canada's cleantech sector, responsible for at least 75 percent of the investment dollars the cleantech sector relies on for its funding. The second is the growing commitment of energy companies to economic reconciliation with indigenous communities. Energy companies understand that they must establish meaningful economic partnerships with First Nations groups to advance new energy projects and build the infrastructure required to support energy diversification and transition. The third is the growing commitment of energy companies to establish and meet increasingly higher and more stringent environmental, social and governance (ESG) standards. The industry is committed to maintaining its top ESG scores among the top 20 hydrocarbon producing nations in the world.

Q. What kinds of risks and challenges are energy executives facing in today's market? How are these factors impacting business activities?

A. Energy executives are facing a number of risks and challenges in today's market, including limited access to capital, inflation and skilled labour shortages. Fortunately, company balance sheets are healthy as commodity prices are anticipated to remain strong for the remainder of 2023. At current market prices, companies have sufficient cash flow to address their competing objectives of maintaining and growing production, paying down debt and repaying investors. Although companies are still exercising capital discipline, we expect to see a material increase in drilling this year. While no significant capital projects in the oil sands are anticipated, oil sands companies are increasing their production through optimisation and debottlenecking activities. The challenge for energy executives is to ensure their companies continue to focus on reducing their greenhouse gas emissions, both on

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an absolute basis, as well as on a relative intensity basis, and that they continue to work toward a net-zero future by 2050.

Q. How do you expect the energy transition to evolve in Canada over the coming years? What opportunities and hurdles does this shift present?

A. While the term 'energy transition' contemplates a transition away from using hydrocarbons as a primary energy source, the International Energy Agency (IEA) acknowledges that global hydrocarbon production will continue to grow for several more years. Since the Russian invasion of Ukraine, the terms 'energy security', 'energy reliability' and 'energy affordability' have become an important part of the global conversion. Canada's oil & gas producing provinces, such as Alberta and Saskatchewan, understand that the world is going to require more energy from all sources for a very long time, and it will take much longer than the next 25 years to transition to non-hydrocarbon sources of energy. Those barrels should be produced by environmentally and socially responsible countries, such as Canada. This sentiment, however, is not fully shared with Canada's federal government, which recently sent the minister of tourism as its representative to Canada's LNG2023 conference in Vancouver, Canada. As a result, significant tensions between provincial and federal policymakers and legislatures have made it difficult to move forward with a unified Canadian energy policy.

Q. What recent, notable energy policies and regulations have been introduced in Canada? What has been the impact?

A. The Canadian federal government has announced a target for Canada's oil & gas sector to decrease emissions by 42 percent by 2030 and a target for Canada's electricity grid to reach net-zero emissions by 2035. These are ambitious goals that are not achievable without significant investment in new capital projects, such as carbon capture and storage, mining of critical minerals and building infrastructure to support the move to electrification. Not only is energy transition expensive, but it will also take time for these projects to obtain regulatory approvals. Unfortunately, the regulatory timelines for permitting the types of projects and infrastructure that will be required are much longer than the 2030 and 2035 target dates, leaving many concerned that meeting these targets will require a cap on the production of hydrocarbons, significantly higher energy costs and a less reliable electricity grid for many Canadians.

Q. Have you seen an increase in restructuring initiatives undertaken by energy and utility companies? If so, what are the underlying drivers?

A. Both the energy and utility sectors are at the heart of the energy transition. Currently, about 80 percent of Canada's electricity comes from renewable or non-hydrocarbon emitting sources, such as hydro, wind and solar. Canada's commitment to move away from coal-fired power generation began in 2012 and in 2022 only 6 percent of electricity produced in Canada was generated using coal. Although Alberta contributes significantly to Canada's generation of electricity from renewable sources, natural gas remains Alberta's pre-eminent source of energy generation. In Alberta, energy

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and power companies are currently looking at participating in carbon capture and storage projects to achieve net-zero goals without compromising reliability. It will be a challenge for those provinces and territories that, like Alberta, rely on hydrocarbons to generate their electricity to meet the federal government's net-zero targets for 2035.

Q. How would you describe M&A activity in the sector? What factors are spurring deals?

A. M&A activity in the energy sector in 2022 was at its lowest level since 2008. High oil & gas prices resulted in significant amounts of free cash flow that companies used to pay down debt and reward their shareholders for their patience through the downturn. With prices stabilising at more reasonable levels by the end of 2022, many were predicting an uptick in M&A activity in the sector in 2023, however by mid-2023 only a handful of deals have been announced. The largest and most significant is ConocoPhillip's acquisition of its remaining 50 percent interest in the Surmont oil sands project from its joint venture partner for C$4bn in cash. With strong cash flows and much healthier balance sheets, energy companies can afford to take more time to strategically consider their allocation of resources and options for growth. As such, industry analysts are not expecting an uptick in M&A activity in the second half of 2023.

Q. What overarching developments do you expect to see going forward? What issues are set to shape energy policy and market activity in the months and years ahead?

A. Canada's energy future will continue to be shaped by the current forces of energy transition, energy security, energy reliability and energy affordability, although not always in equal part, or in equal measure. We expect to see continued legislative, policy and regulatory tensions between the Canadian federal government and the hydrocarbon-producing provinces. These policy tensions create uncertainty for investors, which increases costs and dampens enthusiasm for proceeding with projects in Canada. Canadian energy policy and market activity is also being shaped by the significant amount of funding available for energy transition projects in the US

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under the Inflation Reduction Act (IRA). Canada simply cannot compete with these kinds of benefits. As a result, Canada may attract less foreign investment into its energy diversification and transition economy as foreign investors look for more economically competitive opportunities in the US. ❑

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