PEMBINA Institute

Waiting to Launch

2024 mid-year update

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Summary

Canadian oilsands companies remained highly profitable in 2023, recording the second-highest year of profits in the last decade. The release of 2024 Q2 financial results indicates that the sector is on pace for another highly profitable year, enabling companies to reach or be on track to reach their net-debt targets. This healthy financial position has triggered some oilsands companies to again return record levels of free cash flow back to shareholders, mirroring significant levels of share repurchases and dividends paid in 2022 and 2023.

These highly profitable years are now complemented by the completion of the Trans Mountain Expansion pipeline. Oilsands producers now have access to diversified export markets and may anticipate narrowed price differentials, signalling that profitability in the sector will further increase. There is evidence that companies are now beginning to allocate capital expenditure to targeted activities aimed at growing production.

While the regulatory filings for the Pathways Alliance foundational CCUS project and Imperial's deployment of its solvent-assisted Grand Rapids SAGD project were a step in the right direction, these represent a very small investment towards the major emissions reduction projects first announced three years ago. Furthermore, progress has stalled in reducing emission intensity; in fact, overall intensity in the oilsands has risen 1% since 2018.

The Pembina Institute continues to support decarbonization efforts in the Canadian oil and gas sector and continues to call on governments to provide strong regulation that will compel companies to reduce emissions. Such regulation would complement existing publicly funded financial incentives for decarbonization technologies, such as CCUS.

Introduction

Since 2022, the Pembina Institute has produced a series of reports entitled *Waiting to Launch: The gap between Canadian oilsands companies' climate pledges and actions*.[1] Since the last update in this series, twelve months ago, there have been important changes to the legislative landscape in Canada which are directly linked to oilsands companies' emissions reduction pledges and publicly funded support for their investments.

In June 2024, the Government of Canada finalized and passed into law its Carbon Capture Utilization and Storage Investment Tax Credit (CCUS ITC), which covers 50% of companies' eligible expenses for capture equipment and 37.5% of eligible expenses for transportation and storage equipment — so long as those expenses are incurred before the end of 2030. The passage of the CCUS ITC was a crucial milestone, given that over the last three years, Canada's oilsands companies have cited the finalization of the CCUS ITC as a key requirement for them to commence meaningful investments in decarbonization projects. With the legislation of the federal CCUS ITC we expect that Alberta will now finalize the Alberta Carbon Capture Incentive Program (ACCIP) as it is intended to align with the federal tax credit and provide an additional grant of 12% for new eligible CCUS capital costs to approved projects.

Also in June 2024, the Government of Canada introduced changes to the Competition Act, which has seen some energy companies, including the oilsands Pathways Alliance and its member companies (Cenovus, CNRL, ConocoPhillips, Imperial Oil, MEG Energy, Suncor), remove sustainability and climate-related disclosures and pledges from their public materials. For more information on some of the emissions reduction pledges and project plans that were previously publicized by the Pathways Alliance following its formation in 2021, please see the other reports in the *Waiting to Launch* series. Nevertheless, despite the recent removal of content from the public domain at the time of writing, the Pathways Alliance's website states that the organization's work regarding Canada's biggest oilsands companies reaching net-zero emissions by 2050 "has not stopped."[2]

Given that it has now been more than three years since the Pathways Alliance work was first announced, we think it is as important as ever to provide independent analysis of the actions Canada's oilsands industry is taking to reduce emissions, especially in the context of the financial supports available to these projects while the financial health of these companies remains strong.

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[1] Jan Gorski and Eyab Al-Aini, *Waiting to Launch: The gap between Canadian oilsands companies' climate pledges and action*s (Pembina Institute, 2022). https://www.pembina.org/pub/oilsands-waiting-launch

[2] Pathways Alliance, "Canada's Competition Act amendments," Are you still committed to reaching net zero by 2050? https://pathwaysalliance.ca/home-page/canadas-competition-act-amendments/

Finances

Oilsands producers remain highly profitable

Since our last *Waiting to Launch* update one year ago, profits in the oilsands sector have remained high (Figure 1). Closing out 2023, Alberta's five largest oilsands companies (Suncor, CNRL, MEG Energy, Imperial Oil and Cenovus, the companies that comprise the Pathways Alliance[3]) recorded the second-most profitable year the industry has ever seen, despite profits dropping 25% since 2022 (which was the industry's most profitable year).

This year looks on track to again be a strong year for oilsands profits. So far, in the first half of 2024, these companies have recorded a profit of $10.6 billion; over the same period in 2023 profits totalled $10.8 billion.

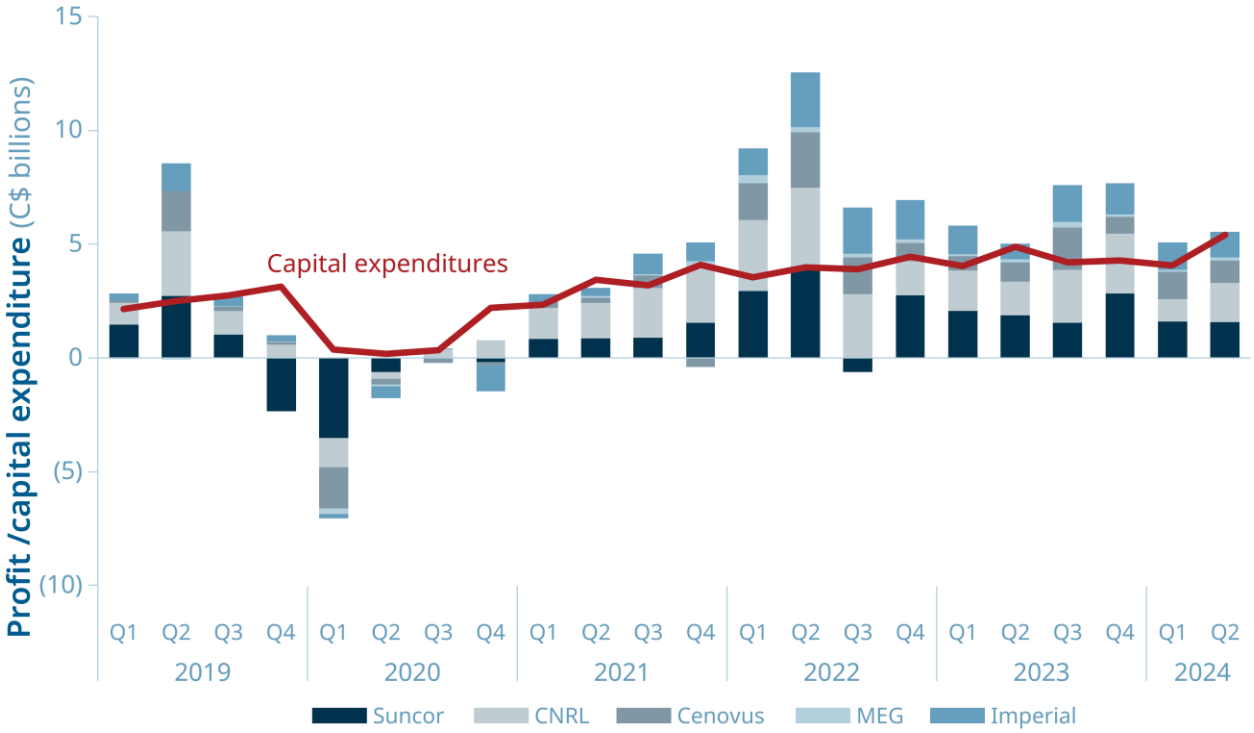

Figure 1. Profits of five of the largest oilsands producers in Alberta

Data source: MarketWatch for historical values up to Q2 2022; Q3 2022 values are from each company's financial statements

With the commercial startup of the Trans Mountain Expansion (TMX) in May 2024 we are likely to see more favourable market conditions for oilsands producers in the near future. Increased export capacity is expected to narrow the price differential between Western Canadian

[3] ConocoPhillips, the sixth member of the Pathways Alliance, was excluded from financial analysis. Although the company produced 81,000 bbls/day of bitumen in 2023, the entirety of its Canadian assets (including conventional oil and gas) make up only approximately 5% of its global production.

Select (WCS) and West Texas Intermediate (WTI), from US$16.90 per barrel in 2024 to US$14.00 per barrel in 2027, according to the Government of Alberta's economic outlook.[4] CNRL, MEG Energy, Cenovus, Imperial Oil, ConocoPhillips and Suncor have committed volumes to the expanded TMX pipeline which will total 890,000 barrels per day (bpd) when at full capacity.[5] The expansion enables increased trade volumes to be exported to the U.S. West Coast and Asia,[6] with some of the first shipments of heavy crude oil shipped through the pipeline being sold to Chinese buyers.[7]

Capital expenditures are now being allocated to new production

Corporate guidance in 2024 remained focused on maximizing value from existing assets, but also shifted to enable some investment in high-value growth opportunities. Oilsands capital expenditures are expected to increase in 2024 after rising an estimated 11% in 2023 from 2022.[8] Suncor intends to increase production 100,000 bpd between 2023 and 2026, congruent with an increase of free funds flow of $3.3 billion.[9] Imperial Oil is bringing on 15,000 bpd from its Grand Rapids project, which saw its first production in 2024. Additionally, Imperial's Leming SAGD project is anticipated to increase production by 9,000 bpd in 2025. Cenovus anticipates an increase in production between 20,000 and 30,000 bpd in late 2025 by connecting its Narrow Lake project to the Christina Lake central processing facility. MEG Energy will begin a $300 million investment in 2024 that will last three years to add 15,000 bpd of new productive capacity at its existing facility.[10] CNRL will add 25,000 bpd production in 2027 from its thermal in situ Pike 1 Project that will begin development activity this year. Meanwhile, with its Horizon project, CNRL is targeting an increase in production of 28,000 bpd in 2025 and an incremental

[4] Government of Alberta, *Fiscal Plan: A Responsible Plan for a Growing Province 2024-2027* (2024), 48. https://open.alberta.ca/dataset/23c82502-fd11-45c6-861f-99381fffc748/resource/3782cc8f-fdc4-4704-9c50-07fc36e05722/download/budget-2024-fiscal-plan-2024-27.pdf

[5] TransMountain, "Past Project: TMEP." https://www.transmountain.com/past-project-tmep

[6] International Energy Agency, *Oil 2024* (2024), 10. https://iea.blob.core.windows.net/assets/493a4f1b-c0a8-4bfc-be7b-b9c0761a3e5e/Oil2024.pdf

[7] Financial Post, "China's Sinochem buys first oil cargo from Trans Mountain Expansion," March 20, 2024. https://financialpost.com/commodities/energy/oil-gas/china-sinochem-buys-first-oil-cargo-trans-mountian-expansion

[8] Alberta Energy Regulator, "Capital Expenditures," Oil Sands Capital Expenditures. https://www.aer.ca/providing-information/data-and-reports/statistical-reports/st98/prices-and-capital-expenditure/capital-expenditures

[9] Suncor, *2024 Business Update*, 9. https://www.suncor.com/-/media/project/suncor/files/investor-centre/business-updates-2024/2024-05-21-business-update-webcast-presentation-en.pdf?modified=20240626203001&created=20240521130737

[10] MEG Energy, "MEG Energy announces 2024 Capital Investment Plan and Operational Guidance," November 27, 2023. https://www.megenergy.com/investors/news-releases/news-release-detail/?id=122731

production increase of 6,300 bpd in 2027 from a $350 million investment in a naphtha recovery unit tailings treatment project.[11]

Notably, ConocoPhillips acquired the remaining 50% interest in the Surmont asset from TotalEnergies EP Canada Ltd., becoming the sole owner in October 2023 for approximately $2.7 billion.[12] Following the acquisition, in December 2023 the Surmont asset achieved first production on its first new pad since 2016.

Free cash flow is being returned to shareholders at record rates

Free cash flow does not have a standardized definition. It is cited by oilsands companies as a measure to demonstrate their efficiency and ability to fund future growth expenditures, pay returns to shareholders and to repay or maintain net debt levels.[13] Oilsands producers continued to generate strong free cash flow in 2023 and have already generated over $9 billion in the first half of 2024 (Figure 2).

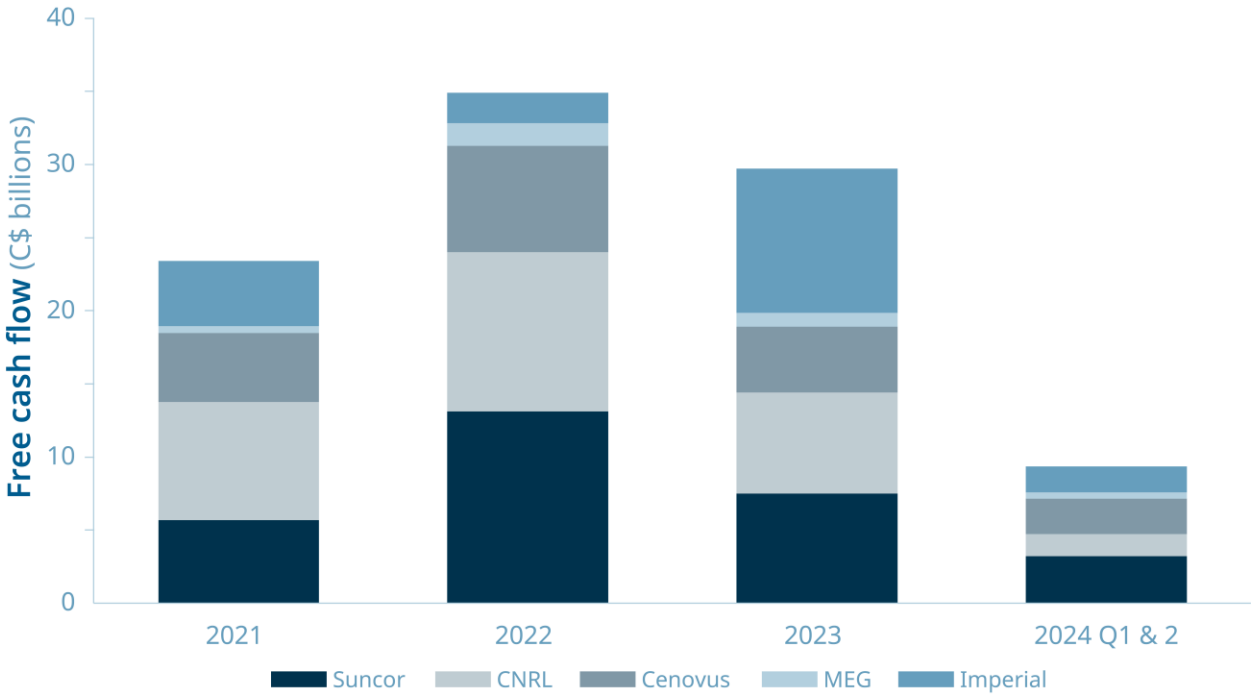

Figure 2. Free cash flow generated by selected oilsands producers

Data source: Values from each company's financial statements

[11] CNRL, "Canadian Natural Resources Limited Announces 2024 Budget," news release, December 14, 2023. https://www.cnrl.com/content/uploads/2023/12/1214-2024-Budget.pdf

[12] ConocoPhillips, *2023 Annual Report,* vi. https://static.conocophillips.com/files/resources/conocophillips_2023-annualreport.pdf

[13] For the purpose of this report, we refer to both free cash flow and free funds flow as free cash flow.

The announcement of second quarter financial results was accompanied by increasing percentages of cash being returned to shareholders. Cenovus announced in August it would be returning 100% excess free cash flow to shareholders. In July, MEG Energy announced its inaugural quarterly cash dividend and the 100% return of free cash flow to shareholders. Cenovus and MEG Energy join CNRL, who has been returning 100% of its free cash flow to shareholders since the beginning of 2024. All three companies have met net debt targets or anticipate meeting them in Q3 2024, triggering these free cash flow allocation plans. Similarly, Suncor increased share repurchases to 75% of excess funds and plans to increase share repurchases to at or near 100%, once its net debt target is achieved.

The combination of factors — capital expenditure now being allocated to production extension projects, net debt targets being reached, free cash flow returns to shareholders and share repurchases reaching record high levels — demonstrates that the sector is maintaining a very strong financial position. As such, it appears appropriately positioned to deploy capital on projects that will reduce emissions, especially given the passage of the CCUS ITC.

Emissions

Oilsands absolute emissions continue to grow, and modest progress on emissions intensity has stagnated

Canada's oil and gas industry, which includes both conventional and oilsands production, is the country's highest-emitting sector, responsible for almost one-third of Canadian emissions annually. Since 2005 — the international baseline year against which Canada's climate targets are measured — all other subsectors (such as conventional oil, downstream oil and gas, and natural gas production and processing) have begun to achieve reductions in their emissions. However, as Figure 3 shows, oilsands emissions have risen 142% in the same period.

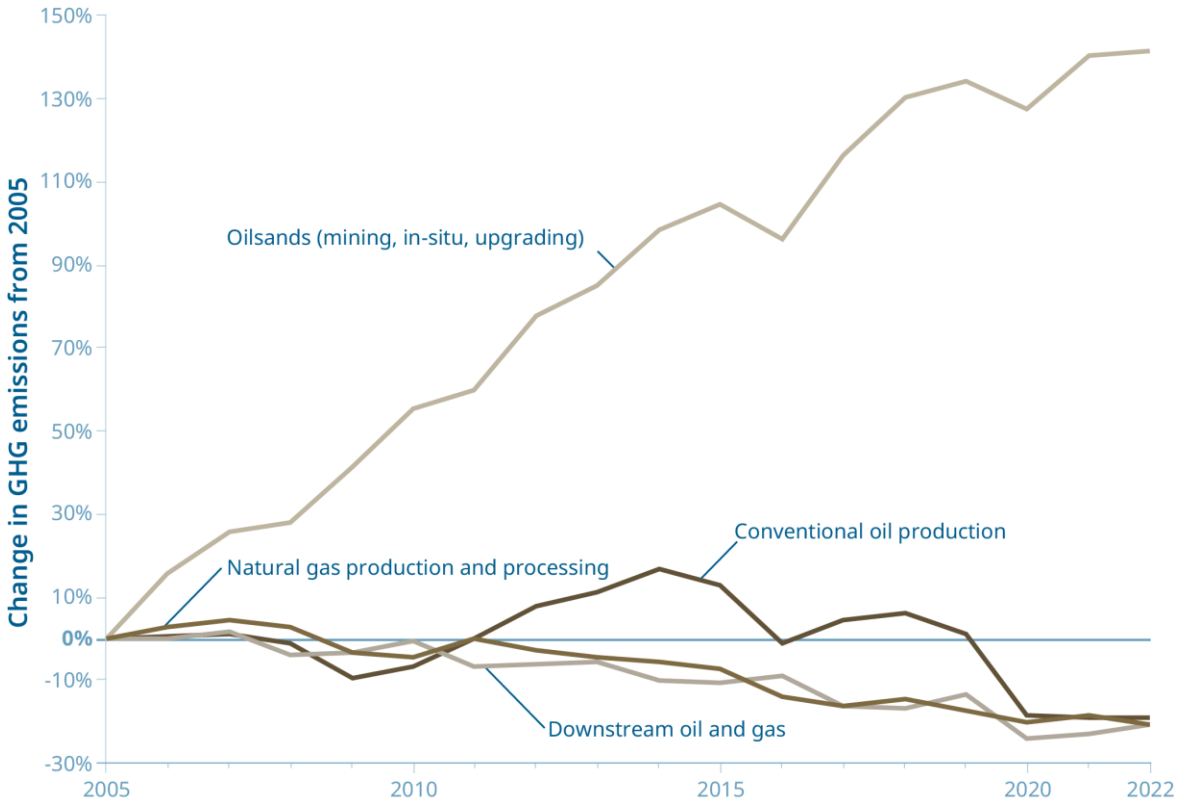

Figure 3. Oil and gas sector emissions trajectory, by sub-sector

Data source: Government of Canada[14]

The oilsands subsector has substantially increased production output during this period (by approximately 211%), which is the driving factor behind absolute emissions growth in the subsector.[15] To communicate its emissions performance, the industry often instead cites gains in emission intensity — the level of emissions per barrel produced. The Alberta Ministry of Environment and Protected Areas also uses oilsands emissions intensity as a performance indicator for whether the government's mandated outcome of sustainable economic development is being achieved.[16]

However, an analysis of emissions intensity since 2011, which is when relevant data first began to be recorded, reveals a more complex picture. As Figure 4 shows, from 2011 to 2022 (latest

[14] Government of Canada, 2024 National Inventory Report (2024), Annex 10: Canada's Greenhouse Gas Emission Tables by Canadian Economic Sector, 1990–2022, Table A10-2. Available at Environment and Climate Change Canada Data Catalogue, "Canada's Official Greenhouse Gas Inventory." https://data-donnees.az.ec.gc.ca/data/substances/monitor/canada-s-official-greenhouse-gas-inventory/B-EconomicSector/?lang=en

[15] Alberta Energy Regulator, *Alberta Energy Outlook: ST98* (June 2024). https://www.aer.ca/providing-information/data-and-reports/statistical-reports/st98/statistics-and-data

[16] Government of Alberta, *Ministry Business Plans*: *Environment and Protected Areas* (2024), 53. https://open.alberta.ca/dataset/23c82502-fd11-45c6-861f-99381fffc748/resource/1c305cf0-658c-48f1-a7ed-a1d38f96cbcc/download/budget-2024-ministry-business-plans-2024-27.pdf

available data), average emissions intensity across the oilsands decreased by 22%. However, since 2018, emissions intensity trajectories across the different extraction methods have diverged. While there have been continued gains from in situ (down 6% since 2018), both mining and mining with integrated upgrade have seen increases in their emissions intensity (by 12% and 8%, respectively). Overall, this means that the average emissions per barrel of oil produced in Canada's oilsands has increased by 1% since 2018 – reflecting a stagnation in these efforts in recent years.

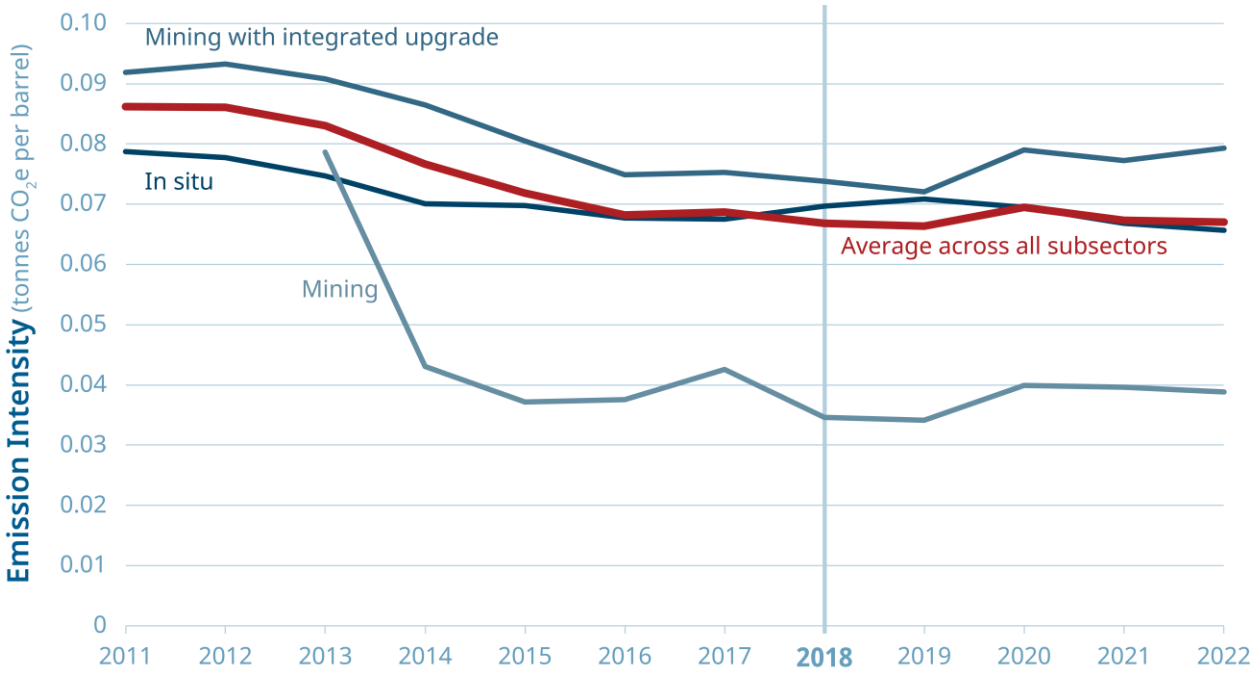

Figure 4. Oilsands emissions intensity by sub-sector

Data source: Government of Alberta[17]

Emissions reduction projects are not moving forward

As previously mentioned, following changes to Canada's Competition Act and greenwashing legislation, oilsands companies and the Pathways Alliance have terminated the voluntary public disclosure of emissions reduction pledges and sustainability reports. MEG Energy has gone as far as suspending its 2030 and 2050 emissions reduction targets until more guidance on the recent Competition Act changes is released. It is unlikely that we will see any significant public discussion of emissions reduction activities or spending until concerns regarding the Competition Act are resolved; however, we do not foresee that the uncertainties that exist with the Competition Act amendments would impact final investment decision announcements.

[17] Government of Alberta, *Alberta Oil Sands Greenhouse Gas Emission Intensity Analysis* (2024). https://open.alberta.ca/opendata/alberta-oil-sands-greenhouse-gas-emission-intensity-analysis

In March 2024, CNRL filed for regulatory approval of the carbon transportation pipeline, which is part of the Pathways Alliance's foundational carbon capture and storage (CCS) project. This was an important step but, as we pointed out at the time,[18] the project is still at an early stage. Given the importance of comprehensive stakeholder engagement — including with Indigenous communities — in the regulatory approval process, the timeline for a final investment decision is now driven by the length of the consultation and approval process.

Pathways Alliance had previously advertised the full cost of its foundational CCS project to be in the order of C$16.5 billion. To ascertain the extent to which this level of spending is being anticipated by the companies, we reviewed the six companies' financial disclosures. Cenovus included a capital spend of $100 million on targeted emissions reduction initiatives over all company operations, which included non-oilsands production as well as the Pathways CCS project, in its 2024 budget update.[19] MEG Energy will be allocating an undisclosed amount of its 2024 capital budget to pre-FEED (front end engineering design) studies for CCS facilities at Christina Lake.[20] CNRL states research and development investment will continue in 2024 and grow in future years with increased participation in the CCS project.[21] Imperial Oil and Suncor state their support for the work the Pathways Alliance is undertaking on the transportation pipeline and carbon storage components but offer no specific information on work they are doing to progress the project. [22,23]

CCUS continues to move forward elsewhere as government supports are finalized

Shell, while not an upstream oilsands producer, approved two carbon capture projects in June, shortly after the federal CCUS ITC was announced: the Polaris carbon capture project and the

[18] Chris Varcoe, "Varcoe: 'A big deal' — Oilsands group files first major regulatory application for $16B carbon capture megaproject," *Calgary Herald*, March 21, 2024. https://calgaryherald.com/opinion/columnists/varcoe-pathways-alliance-oilsands-regulatory-application-ccus-megaproject

[19] Cenovus, "Cenovus announces 2024 budget," news release, December 14, 2023. https:/www.cenovus.com/News-and-Stories/News-releases/2023/2796091

[20] MEG Energy, "MEG Energy Announces 2024 Capital Investment Plan and Operational Guidance," news release, November 27, 2023. https://www.megenergy.com/investors/news-releases/news-release-detail/?id=122731

[21] CNRL, "Canadian Natural Resources Announces 2024 Budget" news release, December 14, 2024. https://www.cnrl.com/content/uploads/2023/12/1214-2024-Budget.pdf

[22] Suncor Energy, *Annual Report*, (2023), 22. https://www.suncor.com/-/media/project/suncor/files/investor-centre/annual-report-2023/2023-annual-report-en.pdf?modified=20240613203824&created=20240321155537

[23] Imperial Oil, "Imperial provides 2024 corporate guidance outlook," news release, December 18, 2023. https://news.imperialoil.ca/news-releases/news-releases/2023/Imperial-provides-2024-corporate-guidance-outlook/default.aspx

Atlas carbon storage hub in partnership with ATCO EnPower. Costs for the projects have not been disclosed. Polaris is projected to capture 650,000 tonnes of carbon dioxide per year from Shell's Scotford refinery and chemical complex. The captured emissions at the Polaris project will be transported to the Atlas carbon storage hub via a 22-kilometre pipeline. This demonstrates that Shell believes the right fiscal incentives are now in place to begin moving forward with its CCUS projects in Canada, and current plans are for these facilities to come online by the end of 2028.[24] However, even with final investment decision (FID) reached on Polaris and Atlas, it is still more than four years before carbon will begin to be captured and stored, and this is only the first phase. An additional phase of the Atlas carbon storage hub, which could store carbon for other companies, will be subject to additional FID. Given the lead times for these projects, it may be worthwhile for other CCS proponents to consider investing in phases for the capture facilities that are most viable and closest to the sequestration hub. In any case, it is a reminder of how little time the Pathways Alliance appears to have left to reach FID and actually begin to capture and store carbon in time to meet its original pledge of achieving significant emissions reductions by 2030.

In addition to Shell's Atlas carbon storage hub, Bison Low Carbon Ventures was granted a carbon sequestration agreement for its Meadowbrook carbon storage hub in August.[25] This makes it the second storage hub in Alberta to receive its sequestration tenure award, which is something the Pathways Alliance will also need in order to move forward with its foundational project.

In July, Strathcona Resources, an in situ oilsands producer in Alberta's Cold Lake region, announced a strategic partnership with the Canada Growth Fund to contribute up to $1.0 billion in project funding for CCS projects at its SAGD facilities in Cold Lake and heavy oil operations in Lloydminster, Saskatchewan.[26] The company has received approval to capture and store carbon dioxide in Saskatchewan and is still working on receiving approval for its SAGD operations in Alberta. While this project has not reached FID yet, it is an indication of the level of public support required for commercial-scale deployment of carbon capture in the oilsands.

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[24] Wallace Snowdon, "Shell gives go-ahead to 2 carbon capture and storage projects in Alberta" *CBC News*, June 26, 2024. https://www.cbc.ca/news/canada/edmonton/shell-gives-go-ahead-to-2-carbon-capture-and-storage-projects-in-alberta-1.7247142

[25] Bison Low Carbon Ventures Inc., "Sturgeon County Carbon Sequestration Agreement granted to the Meadowbrook Carbon Storage Hub Project," news release, August 7, 2024. https://static1.squarespace.com/static/61d72b07c04d092970089446/t/66c2a21eaa1b5e6155ae5845/1724031518414/Meadowbrook+CSA+announcement_Aug+7+2024.pdf

[26] Canada Growth Fund, "Canada Growth Fund Announces up to $2 Billion Carbon Capture and Sequestration Partnership with Strathcona Resources," news release, July 10, 2024. https://www.cgf-fcc.ca/content/documents/Project-Trailblazer-PR-final-for-distribution-EN.pdf

Other emissions reduction activities are starting to develop, but meaningful deployment still lags

Aside from the foundational CCS project, the Pathways Alliance and its member companies have in the past indicated an intention to also pursue other unnamed emissions reduction projects by 2030.

Suncor's fuel-switching project, which began construction in 2019 at its Base Plant operations, is expected to be fully online in late 2024. This will see three coke-fired boilers being replaced with two natural gas cogeneration units.[27]

Imperial Oil achieved the first oil production at its Grand Rapids SAGD project in May, the first to deploy solvent-assisted SAGD in the Canadian oilsands. This technology has been long touted as an effective means of reducing emissions by up to 40% compared to legacy processes.[28] While the Grand Rapids project is in fact an additional production source and will therefore not decrease Imperial's absolute emissions, it should lower the relative emissions intensity of in situ production and lead to further deployment of the technology on existing assets. Imperial is also moving forward with Canada's largest renewable diesel facility at the Strathcona refinery near Edmonton, a $720 million dollar project that will produce 1 billion litres of renewable diesel annually.[29] While this project also will not reduce absolute emissions in the oilsands sector, it is a notable investment in reducing the emissions intensity of fuel.

CNRL has begun piloting its solvent enhanced oil recovery technology on targeted in situ assets and targeting commercial-scale solvent injection in mid-2024 at Kirby North.[30] It also allocates $48 million in its 2024 budget to a naphtha recovery unit tailings treatment project that will reduce GHG emissions by approximately 6% of the Horizon project's total Scope 1 emissions.[31]

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[27] Suncor Energy, "The benefits of fuel switching" March 25, 2024. https://www.suncor.com/en-ca/news-and-stories/our-stories/the-benefits-of-fuel-switching

[28] Imperial Oil, "Imperial Oil achieves first oil production from Grand Rapids project using lower emission technology," news release, May 22, 2024. https://news.imperialoil.ca/news-releases/news-releases/2024/Imperial-achieves-first-oil-production-from-Grand-Rapids-project-using-lower-emission-technology/default.aspx

[29] Amanda Stephenson, "Imperial Oil remains confident in renewable diesel project," *The Canadian Press*, August 5, 2024. https://globalnews.ca/news/10682065/imperial-oil-renewable-diesel-project-update/

[30] CNRL, "Canadian Natural Resources Limited Announces 2023 Fourth Quarter And Year End Results," news release, February 29, 2024. https://www.cnrl.com/content/uploads/2024/02/0229-Q423-Front-End.pdf

[31] CNRL, "Canadian Natural Resources Limited Announces 2024 Budget," December 14, 2023. https://www.cnrl.com/content/uploads/2023/12/1214-2024-Budget.pdf

Conclusion

The Canadian oilsands industry remains in a strong financial position, characterized by what is shaping up to be another highly profitable year, enabling debt reduction, high shareholder returns, and evidence of some investments in increased production capacity. These conditions are anticipated to continue with the recent completion of the TMX pipeline, which is expected to improve price differentials and therefore have a further positive impact on the profitability of Canadian oilsands production.

However, as our research and analysis shows, this extremely healthy financial position that the sector now finds itself does not appear to be enabling investments or allocations of sufficient capital towards emissions reduction activities, including the Pathways Alliance's foundational CCS project. This is also despite the existence of a suite of publicly funded tools designed to support such investments, the finalization of which appears to have spurred other oil and gas companies to begin to move forward with their carbon capture projects in recent months. Time is now quickly running out for Canada's largest oilsands companies to deliver on the emissions reduction pledges they originally laid out in 2021 — pledges that they continue to claim they are actively working to achieve.

This matters because the oilsands is now by far the country's highest-emitting sector; these companies' operations alone are responsible for approximately 12% of Canada's overall annual emissions. As production grows, these emissions will only grow further. At present, it appears Canada lacks a mechanism at either the federal or provincial level to compel companies to take steps to significantly reduce their emissions. This is one reason why the Pembina Institute supports current government efforts to reduce oil and gas emissions, including regulations that complement existing financial incentives. Given the urgent need for a global shift to lower-carbon energy systems, and the importance of the oil and gas sector to Alberta's economic stability and Canada's export balance, we will continue to support these efforts to enable an orderly transition.

The Pembina Institute acknowledges that the work we steward and those we serve span across many Nations. We respectfully acknowledge the space our organization is headquartered in as the traditional and ancestral territories of the Blackfoot Confederacy, comprised of the bands Siksika, Piikani, and Kainai, the Îyârhe Nakoda Nations, including the bands of Goodstoney, Chiniki, and Bearspaw, and the Tsuut'ina Dené. These Lands are also home to the Métis Nation of Alberta — Region 3 whose Peoples have deep relationships with the Land.

These acknowledgements are some of the beginning steps on a journey of several generations. We share them in the spirit of truth, justice, reconciliation, and to contribute to a more equitable and inclusive future for all of society.