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## ALBERTA'S OIL WOES SPREAD BEYOND THE ENERGY INDUSTRY

Provincial government plans to slash spending and could raise taxes. It's no secret the steep decline in oil prices are having a significant impact on Canada's energy industry.

But the drop in the commodity price is affecting those outside the sector, who rely on resource revenues to help fund new schools, transit and other projects and services.

Tomoko Vishnu wakes before 6 a.m. each weekday to make a lunch and pack a school bag for her 10-year-old son, before he catches the bus for a 40-minute ride to school. A trip she had hoped her kids would never have to make.

"We bought this house because it said a school was going to be built in this neighbourhood. That's why we bought this house here," she says.

That school was supposed to be built just a five-minute walk from Vishnu's house in southeast Calgary. It is supposed to open next year, although she says there is still no sign of it. Adding to her concerns, the

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provincial government is reviewing all capital projects, including hospitals, schools and highways.

"Nothing is happening right now and I am just hoping that it's not going to affect anything like a budget cut for the school because it has already been a lot of stuff cut," she says.

The price of oil has plummeted from

highs of more than \$100 less than a year ago to around \$50 today. That has had a huge impact on Alberta's energy industry, which has seen companies slash spending and shed employees. But it also hurts the provincial government, which counts on energy royalties for about 20 per cent of its revenue.

"The fact of the matter is, when you have a \$7-billion hole in your budget some decisions are going to have to be made and it's going to affect decisions across the board," says Alberta's Finance Minister Robin Campbell, who has put all capital projects in the province under scrutiny. That includes a proposed cancer

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treatment centre in Calgary. The facility was approved by former premier Alison Redford to be built by 2020. That timeline no longer seems plausible.

"Why in a matter of months do we go from the 'have' province that everyone admires to a province that has these incredible budget challenges that means we can't be a modern, progressive province that can look after its citizens," says cancer survivor John Osler, who is part of a group pushing to have the centre built.

The answer is simple, according to University of Calgary political scientist David Stewart; Albertans

have chosen a government that relies too heavily on energy royalties and too little on tax revenue.

"If Alberta taxed at the level of the next lowest province, not the provincial average, it would bring in \$11.6 billion in additional revenue and that would make all of this go away," he says.

Of course that is easier said than done.

Many Albertans cringe at the possibility of higher taxes, proud to be the only province without a sales tax. But some people would be open to the idea.

"I have got no problem with a sales tax, but I understand that is a hard sell for Albertans," says

Adam Johnson, who spends 90 minutes a day taking a crowded bus between a Calgary suburb and his downtown oil and gas job.

"Calgarians are demanding a train, now we are demanding someone to pay for it," he says.

Johnson would like to see a proposed light rail line project become a reality. The city would need significant provincial funding before ever breaking ground.

When the province could be in a position to pay for that train, or any other infrastructure, will become a little clearer next month when Alberta's budget is released.

But in Canada's energy capital, the fate of many projects will likely continue to hinge on the price of a barrel of oil.

### FRACKING FIRMS CUT SALARIES, PARK EQUIPMENT, SNIP COSTS

Calfrac Well Services Ltd. is reducing its budget, directors' fees and executives' salaries — and will pack up and leave Colombia entirely — to deal with a global oil patch slowdown due to huge cuts in the budgets of its energy producer customers.

The cuts announced Wednesday



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came as the Calgary-based oilfield services and hydraulic fracturing company reported record fourth-quarter revenue of \$749 million, up 62 per cent over \$463 million in the same period of 2013, as it performed 41 per cent more fracking jobs and revenue per job increased by 16 per cent.

After markets closed, rival Trican Well Service Ltd. reported it, too, had buoyant revenue in the fourth quarter of 2014 but it, too, would cut salaries, fees and costs and had already reduced its North American workforce by 600 positions.

Calfrac said operating income

more than doubled in the last three months of 2014 from the year-earlier period to \$122 million.

But president and chief executive Fernando Aguilar said on a conference call with analysts that low crude oil prices are affecting Calfrac's equipment utilization and pricing in the first quarter of 2015.

"As a result of the decline in crude oil prices, the company's customers in Canada and the United States have lowered their 2015 capital budgets in the order of 20 to 40 per cent from 2014," he said. "Customers are taking a cautious approach until there is more certainty as

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to when oil prices will recover."

Calfrac said it will cut more than \$25 million from general and administrative costs this year, including a 20 per cent reduction in directors' compensation and 10 per cent from executive salaries effective April 1. It also plans to reduce stock-based compensation and annual bonuses.

It said it will restructure the organization at all levels for expected activity in 2015, work with suppliers to reduce input costs and vowed to park equipment rather than run it with insufficient profit margins.

It will also evaluate underperforming regions and services lines, noting it has closed a coiled tubing operation in Pennsylvania. It announced it had decided to exit Colombia and would remove its three cementing units there, and had rationalized its Mexican arm, relocating half of the fracturing horsepower to the United States to be parked.

Calfrac set its 2015 capital budget at \$215 million, which includes about \$175 million of carryover capital from last year. It said it had been able to defer or cancel about \$30 million from its \$360-million 2014 capital program. New capital



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of about \$40 million this year will go to maintenance, infrastructure and sustaining operations.

The company intends to deliver 140,000 horsepower of fracturing capacity in mid to late 2015.

Shares closed down nine cents at \$9.15 on the Toronto market Wednesday. In the past 52 weeks, they've ranged between \$7.28 and \$22.57.

Analyst Dana Benner of AltaCorp Capital said in a note to investors that Calfrac's fourth-quarter adjusted earnings per share were 51 cents, beating AltaCorp's and consensus expectations of 44 cents. Revenue beat forecasts by more than \$80 million.

"The revenue beat was largely due to strong results across Canada, the U.S. and Latin America while

Russia missed as a result of the declining ruble," he wrote.

In its release, Trican said that effective Feb. 1, it had cut average compensation by 10 per cent for all of its Canadian, U.S. and corporate employees, including a 15 to 18 per cent reduction for senior executives and a 15 per cent reduction in director compensation.

It said the reductions would result in savings of \$15 million in Canada, \$10 million in the U.S. and \$3 million for corporate division.

Trican reported fourth quarter revenue of \$755 million, up from \$552 million in the same period of 2013, and operating income of \$105 million versus \$36 million a year earlier. Net income was \$4.9 million.

It also took note of the sharp decrease in activity in Canada and the United

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States, predicting that the traditional spring breakup north of the border will start earlier and end later this year for economic reasons. It said it expects prices to fall 10 per cent by March 31 and that it will park 20 to 25 per cent of its Canadian pressure pumping equipment by then.

It added it has already parked a fracturing crew in each of its Eagle Ford, Bakken, Permian and Longview regions this year and has closed its operating base in Longview, Texas, where one fracturing crew and two cement

crews had previously operated.

**LULL IN ALBERTA OIL PATCH FREES UP CHARTER JETS FOR DISCOUNTED FLIGHTS**

A slowdown in demand for charter flights in Alberta's oil patch has freed up planes for a marketing company to resume Calgary-Vancouver trips and introduce discount rides on the Calgary-Toronto route.

Roger Jewett, the chief executive officer and founder of Jump On

Flyaways, said the firm is able to offer large savings on airfares to consumers because it hires idle charter aircraft at low rates. There is a catch to the offerings, however, and it is a big one – unless Jump On fills roughly three-quarters of the available seats on a route, the proposed flights featuring deeply discounted fares will be cancelled.

“Our flights go if we sell enough seats. We only go if we hit the jumping point, which is basically break even or better,” Mr. Jewett

said in an interview Monday. Jump On has flown the Calgary-Vancouver route in the past, notably during Grey Cup weekend last fall in Vancouver.

The next quest is to fill as many seats as possible for flights between Calgary and Vancouver over the Easter long weekend in early April. Jump On’s round-trip flight on the Calgary-Vancouver route has been priced at \$248. The airfares are roughly 50 per cent lower than the rivals’ typical weekend

ticket prices for a trip originating in Calgary, Mr. Jewett said.

Passengers have the option to make charter bookings for \$124 one-way through Jump On, and pay WestJet or Air Canada for the other flight segment on scheduled service.

So far, tickets are selling briskly for the 148-seat flight originating in Calgary on April 2, but sales are slow for the trip starting in Vancouver that same day. The return flights on are April 6. Jump On has a limited number of seats on sale for \$99 one-way from

Vancouver to Calgary on April 2, and from Calgary to Vancouver on April 6.

Persuading Calgarians to book to Vancouver has gone smoothly so far for Jump On, and the challenge will be filling seats with Vancouver residents in early spring. WestJet and Air Canada are offering deals as low as \$169 one way in early April to stimulate demand for Vancouverites to visit Calgary, but Mr. Jewett said his firm provides cheaper seats for all passengers.

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Jump On has managed to forge ahead with 10 round trips on various routes, or a 50-per-cent success rate for attracting enough passengers. Mr. Jewett wants to ramp up the number of trips and destinations offered in 2015, and expects that the success rate will increase over time as more consumers get used to booking on Jump On's website.

On the Calgary-Toronto route, the proposed launch dates will be around the May long weekend, but possibly earlier.

## LNG EXPORTS FROM CANADA A DISTANT PROSPECT, ANALYST SAYS

Energy economist Kenneth Medlock says Canada's projects are too expensive to compete

The ship has already sailed in the global race to export liquefied natural gas to Asia, according to U.S. energy economist Kenneth Medlock — and Canada has missed it.

Medlock was a keynote speaker at the Canadian Energy Research

Institute's annual conference on natural gas. This year the conference was called LNG: Canada's Last Window of Opportunity.

That title reflects the simmering anxiety among natural gas producers in Western Canada that the opportunity to sell their natural gas to Asia is slipping away

The anxiety is well-founded, according to Medlock.

"We don't see any LNG exports from Canada until almost 2040," he said in an interview.

Medlock expects almost all new LNG supply to come from the United States or Australia.

The largest issue is cost. Canadian projects are green field, meaning they are being built from scratch.

In the U.S., multiple projects are conversions of existing LNG import terminals that already have ports built and pipelines attached. They simply need to be converted so they can export instead of import.

"The fixed cost to get them finished is relatively low," said Medlock. "That serves a distinct advantage."

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Medlock expects four of those terminals, including Maryland's Diamond Cove, pictured above, to come online soon, as well as several Australian projects.

"That's going to cause a lot of softness in the market and cause a lot of developers to put the brakes on things.

"That's the capacity that's coming — it's already steel on the ground, so it's happening — and the market is just not going to be substantial enough to absorb it all in a very short period of time. It's a classic boom-bust cycle."

Once that capacity comes online, Medlock expects, Asian LNG prices will drop to the point where Canadian facilities are no longer viable.

Because international prices for LNG are linked to the price of oil, they have come down considerably since August. The Japanese benchmark was trading close to \$15 US per million British thermal units (MBTUs) to under \$7 US. That's not enough to make shipping LNG from North America profitable for anyone right now.

Peter Howard, president emeritus of the Canadian Energy Research Institute, said he's done the same math as Medlock but come to a different conclusion, as long as oil prices recover to \$70 US per barrel.

"We took into account the Qatari gas and all the Australian projects that are under construction or completed construction," said Howard.

"We added into that the Gulf of Mexico and that left room in 2020-23 for two additional projects, which we think are the West Coast projects."

Howard said that also assumes that Japan would bring most of its nuclear power industry back online soon, something that he said seems increasingly unlikely. Most of Japan's nuclear plants have been disabled since the Fukushima reactor meltdown in 2011. If they remain out of commission, Japan will depend more on fossil fuels such as natural gas.

According to the B.C. government, there are 19 proposed LNG projects. Many have been granted export licences, but none have made the final investment decision.

That comes from the board of directors of each company, a decision to spend tens of billions of dollars on a project. It's not an easy decision to make, especially with oil prices on the skids.

Malaysia's Petronas has delayed its final investment decision on its \$36-billion project. Chevron has slowed spending on its project in Kitimat. Shell is hoping to have a decision this summer

on its \$40-billion Kitimat project.

In mid-February, the federal government helped things along, by announcing a tax break for the proposed LNG facilities, allowing them to write down their multibillion-dollar investments more quickly. That was a key piece of the investment puzzle.

The other piece of the puzzle is the price of oil, which is expected to start recovering later this year, according to Judith Dwarkin, chief energy economist at ITG Investment Research in Calgary.

Dwarkin agreed with Medlock's general argument that Canadian projects face headwinds, particularly around how much they cost. But she said the projects shouldn't be counted out.

"I would hesitate dismissing completely the possibility of any Canadian LNG plying the waves in the next 25 years," said Dwarkin.

"There are price scenarios and tolling agreements that conceivably could make sense. And Asian buyers supposedly value diversity of supply, a box Canadian LNG checks off."

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