A crude awakening

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>
> *— Lynn Westfall, co-author of "The Effects of Removing Restrictions on U.S. Crude Oil Exports"*

One of the hottest topics in Washington DC right now is the crude oil export ban. This topic has been picking up

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steam for the past five years and is now appearing to reach a major milestone decision in the next few months.

Last week, the Energy Information Administration released a study explaining how the world would look if we exported crude oil overseas. One of the authors, Lynn Westfall, believes this study offers a non-industry look at the topic and will shed some light on the subject. Westfall also served as an advisor to the model on the effects on the mining industry.

Westfall has first-hand knowledge and is familiar with the oil and gas industry in North Dakota and the Bakken.

"I was in industry for 35 years, I have only been working in government for 2 years," Westfall said. "I used to work for Tesoro that owns the refinery in Mandan. I know North Dakota very well."

When asked about his opinion on the recent opening of the Dakota Prairie Refinery, the first greenfield refinery opening in the United States since 1976, Westfall said it makes sense for North Dakota but wasn't sure if it would work anywhere else.

"That particular one seems to make a lot of sense," Westfall said. "As you know, North Dakota get[s] very short on diesel fuel during times of the year and there really is no place to bring it in from inexpensively."

Westfall suggested the nation's supply of refineries is currently fulfilled while North Dakota was an anomaly in the refinery world.

"Mostly we don't need more refineries in the United States," Westfall said. "North Dakota is a particularly unique set of circumstances where it makes sense."

Transitioning back to the report, officially titled "The Effects of Removing Restrictions on U.S. Crude Oil Exports", Westfall reminds there is not an export ban, just restrictions.

"There really isn't an export ban, just restrictions. For example, we can export all we want to Canada. Which we have been doing," Westfall said. "We can export ANS crude, California crude. There isn't a ban, just restrictions on what kind of crude and where you can export it."

Westfall said the debate has been discussed since the "fracking revolution" began, and centers around two concepts.

"The first issue is with all this new domestic crude production coming on field is domestic producers getting the full international price for the crude," Westfall said. "The answer to that is: it depends."

Westfall explained and offered context to the study and projected results.

"Because if they are not getting the full international price, then ending the restrictions would allow them to get a higher price which allows them to produce more," Westfall said. "And the reason they may not be getting the full price by selling it in the US is because US refineries are not really geared to run that type of crude. They are geared to run heavy crude."

Explaining the study further, Westfall said a number of factors and numbers had to be included.

"We looked at a whole range of production in the United States and basically what we found was, up to about 11.5 million barrels a day, the US refining system can handle and pay full price," Westfall said. "Once you reach about 11.5 million barrels a day, which is roughly 2 million more barrels a day than we are producing right now, then you reach a point where domestic refineries have a real problem running that light crude and the price has to be discounted pretty substantially to incentivize refineries to add capacity to run light crude."

When comparing the Brent and WTI discounts, national versus international, Westfall said the discount is about $4-a-barrel. However, in the study's most restrictive case, that discount could go up to $14-a-barrel by 2025.

"That's if you don't end the restrictions," Westfall said. "If you keep producing and forcing it into US refineries because you cannot get it into the international market, you reach a breaking point of about 11.5 million barrels a day and the refineries have to get a discount because they cannot really run that crude, and they have to build new units in order to run it."

Bottom line for the Bakken: Will lifting the restrictions or ban impact the Bakken's sweet crude?

"Only if you assume production will reach 11.5 million barrels a day," Westfall said.

When asked if $100 or $30 oil prices will impact the study's finding, Westfall explained price really isn't a major factor. "In our view it isn't so much about prices, which we believe prices will be in the $60s or $70s, but in our mind the difference between a low production case and a high production case is more around the resources you can bring to bear," Westfall said. "Rigs, people, recovery rates, drilling rates, those sort of things."

Westfall said assuming all those energy operational duties are achieved, the 11 million mark will be reached in 2020.

The second issue hinges on the first: if the producers are not getting full value and we lift the restrictions and that raises domestic crude prices, will that raise gasoline prices?

According to Westfall, gasoline prices will not be negatively impacted by the lifting of the crude oil export restrictions.

"We put out a study a year ago that definitively showed that US gasoline prices are tied to international crude prices, not domestic," Westfall said. "We can freely import and export gasoline, which we do in the United States, so it is really an internationally priced commodity, not local priced. So regardless what you do with domestic prices, it does not affect gasoline."

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