Joel Moser Contributor

I cover investment in energy and infrastructure.

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Who Killed The Keystone Pipeline -- And Why Nobody Cares

Here's the headline story: the backers of the Keystone XL pipeline, TransCanada, withdrew their application just ahead of an expected permit denial by the Obama administration. This is being cast as a victory by environmental activists who have opposed this project, about which *The New Yorker* exclaimed, "Essentially, it's game over for the planet."

Credit the environmentalists for the delay, but the victory probably goes to a far more effective player: the Market. While I don't pretend to be an Oval Office mind reader, it is noteworthy that the articulation of negative views on this project came not at the height of the fracking boom, when it was widely thought that America's unconventional energy industry would lead the country out of recession and to ultimate energy independence, but rather as Goldman Sachs was predicting $20 a barrel oil, a level that would idle not only the shale fields of North Dakota but also the oil sands of Alberta.

Most savvy observers fully expect oil prices to recover to a point that production in Canada and the Bakken will be profitable, just less so. Current prices are seen as a short-term supply overhang. This is probably correct. However, oil prices have not been behaving as predicted lately, and at current price levels, there exists a fair question as to whether such an expensive bit of infrastructure makes sense to build at all, at least right now. Because here's the financial problem with infrastructure: it's capital intensive and the business models typically require very long life economic returns.

So absent long-term take-or-pay contracts, commodity price risk is a total buzz kill for infrastructure investors. Back when oil prices floated above $100, the risk that the entire Canadian oil business could be mothballed seemed remote. Right now, it seems within the range of possibility during the 20 to 30 years required to amortize a massive infrastructure investment.

I expect that Keystone will be back for a federal permit when prices are back to the $70 range required to make the North American unconventional oil industry profitable again. But note to the environmentalists: the best way to keep carbon in the ground is to develop cost effective alternative energy solutions, not lobbying. The Market usually wins.

The Keystone Steele City pumping station, into which the planned Keystone XL pipeline is to connect to, is seen in Steele City, Neb., Tuesday, Nov. 3, 2015. TransCanada, the company behind the project, said Monday it had asked the State Department to suspend its review of the Canada-to-Texas pipeline, citing uncertainties about the route it would take through Nebraska. (AP Photo/Nati Harnik)