Greetings,

Key conclusions from the latest assessment of oil markets by Raoul LeBlanc, vice president, financial services and the IHS Markit Energy Advisory Service follows. Please feel free to quote from below.

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“Great Shut-in” Hits North America—U.S. Oil Producers to Halt 1.75 Million Barrels Per Day of Production

Canada expected to cut half a million barrels per day also as “Great Shut-in” takes hold

Due to the collapse in oil prices, IHS Markit expects U.S. producers are in the process of curtailing about 1.75 MMb/d of existing production by early June due to operating cash losses, lack of demand and storage capacity, and an unwillingness to sell resources at the very low prices available since the onset of the COVID crisis.

These reductions are not permanent. IHS Markit has projected a return of most curtailed volumes in the summer and fall of 2020 as tightening fundamentals lead operating margins back to positive territory. This resumption of production may accelerate if WTI remains above $30 per barrel—a price that allows operators to cover their operating costs and that reflects improved storage availability.

However, about one third of the volumes (approximately 550,000 b/d) will stay off the market for the long-term—or at least until WTI prices push above $50/bbl, justifying the capital spending needed to repair the impact that some of the wells will have incurred from being shuttered.

“*The oil market fear that characterized March and the extreme price pressure that producers felt in April have galvanized producers across North America into unprecedented action.*

“*Not even the United States’ huge network of storage facilities and associated infrastructure was enough of a buffer for a crisis on this scale. Negative oil
prices and the collapse of WTI futures contracts were a potent signal that stronger measures, namely shut-ins, were needed to curb oversupply.” – Raoul LeBlanc, vice president, financial services, IHS Markit

In the United States, the expected curtailments go well beyond just low-productivity conventional wells, known as “stripper wells.” Those wells, which produce less than 5 barrels per day of oil and more than 35 barrels of water which must be reinjected to maintain reservoir pressure, are expected to make up 350,000 b/d of the reduction.

However, nearly 1.4 MMb/d of the reductions are expected to come from relatively prolific shale wells. IHS Markit expects the bulk of the cuts to avoid the newest of the wells and focus on production from those with established production histories.

Canada, hit by its own economic and storage issues, is set to cut an additional 500,000 b/d from its production. Much of this reduction will come from oil sands projects, which have a set of options, handicaps and interdependencies that differ from other asset types.

For producers, the unique characteristics of the North American market play a prominent role in the decision of which wells to cut:

- **Private ownership of mineral rights**: The United States onshore is the only major producing area in the world with primarily private ownership of petroleum mineral rights. In all other parts of the world, governments own the resource and thus have far greater control of petroleum operations—despite contractual commitments with international operators. Private ownership involves a complex web of legal implications for hundreds of thousands of individual lease contracts and millions of stakeholders.

- **“Integration” of the flow of molecules**: More than 80% of North America's output of 36 million barrels per day of oil equivalent flows into domestic industries to be gathered, processed, refined, re-fashioned, purified, or burned to generate power. This level of integration means that decisions to shut-in wells have complex downstream consequences across multiple industries.

- **Disintegration of oil and gas companies**: Although the molecules may be integrated, the North American corporate landscape is decidedly disjointed. Over the past decades, the industry has specialized. This has been, by and large, a very successful division of labor, creating a highly efficient and lean chain that is flexible when dealing with routine volatility. However, "black swan" events (such as pandemic-induced economic shutdown) expose the challenges of such lean, optimized systems.

- **Large storage capacity and transport fungibility**: A final factor that makes the US different is its abundant storage capacity and ability to relocate oil and gas through its dense pipeline network. This optionality to store allowed US producers to avoid shut-
ins from early March through mid-April, when producers in other countries were already seeing their supply chains seize up. However, not even the US' huge network of storage facilities and associated infrastructure was enough of a buffer for a crisis on this scale. Nevertheless, U.S. producers will have more flexibility as the storage crunch fades.

"North America has, by far, the greatest number of producers (15,000-plus) and producing wells (more than one million), as well as the greatest diversity of subsurface conditions and operational technologies. This creates immense optionality within the system as companies evaluate and execute the mass shut-ins in response to the market." – Raoul LeBlanc, vice president financial services, IHS Markit

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