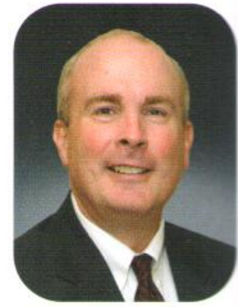
Percussa Resergo



By John Harpole

Every once in a while, we need a bit of Latin to boil things down; and the phrase "percussa resergo," which means "being struck down I rise again," perfectly captures the past four decades of the domestic oil sector.

Consider this stunning fact: The U.S. is poised to overtake Saudi Arabia as the world's top oil producer. Last year, 50% of the world's growth in oil production came from the U.S. According to the American Petroleum Institute, in 2012, U.S. oil production increased by 779,000 barrels (bbl.) per day, or 13.8%. In 2012, U.S. oil production saw its largest annual increase in history.

What's been the catalyst? The free market is very efficient at eliminating crude oil price differentials between places like Hardisty, Alberta (Western Canadian Select); Cushing, Oklahoma (West Texas Intermediate or WTI) and the North Sea (Brent).

Producers deserve the lion's share of credit for the upsurge in produced oil volumes. However, midstream crude marketers deserve some praise. Their ingenuity in railing crude oil out of pipeline-curtailed producing regions was marketing innovation at its finest.

Oil pipeline solutions require long lead times for construction, and long-term contractual commitments (one- to five-year contracts for rail compared to 10-15 years for pipelines). Oil by rail can be quickly deployed at a lower cost for a shorter term and can be redirected with three days' notice to a producer's market of choice.

The surge in oil moved by rail would no doubt make the great economist Friedrich Von Hayek smile. He stated, "Competition means decentralized planning by many separate persons."

Hayek would note that the surge in oil moved by rail is shrinking the price spreads across the popular trading hubs. Those price spreads serve as an extremely efficient mechanism for the communication of information. Those price spreads did not fall on deaf ears.

Hayek might have had business partners Jack Galloway, Erik L. Johnson and their colleague Dan Dempster in mind when he referred to "separate persons." Galloway and Johnson formed Canopy Prospecting Inc. to chase a dream to keep south Philadelphia vibrant.

In September 2011, Sunoco and ConocoPhillips announced plans to sell or close three Philadelphia-area light, sweet crude refineries. Canopy thought it would be a pity to, "disassemble the refineries and move them to India like so many other former U.S. process plants." They considered a number of options and were finally encouraged to "make it more viable for the refineries to operate as refineries."

Could North Dakota's Bakken oil beat the cost of North Sea Brent crude for area refineries?

Johnson shares the moment of epiphany: "We quickly reached a conclusion that the three Philadelphia-area refineries up for sale could be very attractive to buyers if they had reliable access to lower cost rail-delivered Bakken crude."

They were the first to "pencil out" and recognize the possibility of unit trains, filled with North Dakota's Bakken oil, making the 1,500-mile trip to South Philly. Each mile-long unit train could hold more than 80,000 bbl., but where to off-load something that long in South Philly?

According to Johnson, they determined that, "the only place to locate a crude oil train unloading facility was in the soon-to-be-closed Exelon Eddystone Generating Station." The sight had excellent marine facilities on the Delaware River, and was within 6 miles of an existing 700,000 bbl. per day of East Coast refining capacity. That refining market, second only in size to the Houston-area refinery market, would be available by transloading oil into barges that would transit the Delaware River.

To their credit, Exelon recognized the potential to keep industry in South Philly alive and granted a lease on its 1950-vintage coal train loop tracks.

Eddystone Rail Co. LLC was born. "Philly Light" sweet crude oil was also born.

Enbridge shared their vision for a "mini-Cushing on the Delaware," and now holds 75% of the Eddystone joint venture (JV). That JV now boasts a $68 million south Philadelphia oil-unit train transloading terminal and distribution facility.

Philly Light crude will be displacing imported North Sea Brent crude oil and foreign imports of gasoline. It's shaping up to be a great Bakken vs. Brent crude oil battle royal along the banks of the Delaware—and the Bakken is winning. Bakken pricing is also narrowing the price gas with WTI crude pricing. In the past 14 months, the $11.11 per bbl. three-month average spread has closed to $3.52 per bbl.

Much like the Bakken, South Philly industry is thriving and has "risen again."

That's a good thing on many levels; it is especially good for American jobs, energy security and balance of trade concerns. ■

***John Harpole** is senior advisor to* Midstream Business, *founder and president of Mercator Energy LLC and a board member of the Western Energy Alliance, Colorado Oil and Gas Association, Leadership Program of the Rockies, University of Colorado's Global Energy Management Program and Energy Outreach Colorado.*