Buffett’s Burlington Northern Among Winners From Keystone Denial

By Jim Efstathiou Jr. - Jan 22, 2012 9:00 PM PT

Warren Buffettôs Burlington Northern Santa Fe LLC is among U.S. and Canadian railroads that stand to benefit from the Obama administrationôs decision to reject TransCanada Corp. (TRP)ôs Keystone XL oil pipeline permit.

With modest expansion, railroads can handle all new oil produced in western Canada through 2030, according to an analysis of the Keystone proposal by the U.S. State Department.

ñWhatever people bring to us, weôre ready to haul,ò Krista York-Wooley, a spokeswoman for Burlington Northern, a unit of Buffettôs Omaha, Nebraska-based Berkshire Hathaway Inc. (BRK/A), said in an interview. If Keystone XL ñdoesnôt happen, weôre here to haul.ò

The State Department denied TransCanada a permit on Jan. 18, saying there was not enough time to study the proposal by Feb. 21, a deadline Congress imposed on President Barack Obama. Calgary-based TransCanada has said it intends to re-apply with a route that avoids an environmentally sensitive region of Nebraska, something the Obama administration encouraged.

The rail option, though costlier, would lessen the environmental impact, such as a loss of wetlands and agricultural productivity, compared to the pipeline, according to the State Department analysis. Greenhouse gas emmissions, however, would be worse.

If completed, Keystone XL would deliver 700,000 barrels a day of crude from Albertaôs oil sands to refineries along the Gulf of Mexico, crossing 1,661 miles (2,673-kilometers) over Montana, South Dakota, Nebraska, Kansas, Oklahoma and Texas.

Tanker Car Bottleneck

Investors such as John Stephenson, who helps manage $2.7 billion for First Asset Management Inc. in Toronto said he anticipated the project would move forward next year. Pipeline shipping costs remain lower than rail, and a lack of readily available tanker cars may create a bottleneck.

The availability of tank cars may create a temporary ñhiccupò in transport capacity, according to Tony Hatch, an independent railroad analyst in New York. Rail cars are ña pretty hot commodity,ò as a result of demand from oil producers in North Dakota, he said.

Rail car production is already at a three-year high as manufacturers such as Greenbrier Cos Inc. (GBX) and American Railcar Industries Inc. (ARII) expand to meet demand for sand used in oil and gas exploration, according to Steve Barger, an analyst at Keybanc Capital Markets Inc. in Cleveland, citing Railway Supply Institute statistics.

‘Long-Term Solution’

Rail-car suppliers can add capacity, Hatch said.

ñRailroads are not just a stopgap while we wait for a pipeline,ò Hatch said in an interview. ñThey are potentially part of the long-term solution.ò

Railroads are being used in North Dakota (STOND1), where oil producers have spurred a fivefold increase in output by using intensive drilling practices in the Bakken, a geologic formation that stretches from southern Alberta to the northern U.S. Great Plains. During 2011, rail capacity in the region tripled to almost 300,000 barrels a day as higher production exceeded what pipelines handle, according to the State Department report on Keystone XL.

Shipping oil using tank cars on rail costs about $3 more a barrel than pipeline transport, using prices in North Dakota, a differential ñunlikelyò to slow the development of oil sands crude if no pipeline is build, the State Department said. The gap is shrinking as larger storage terminals are built, the agency said.

‘Ready to Haul’

Burlington Northern carries about 25 percent of the oil from the Bakken, said Krista York-Wooley, the railroad spokeswoman. The company can carry higher volumes from North Dakota or Alberta, she said.

Canadian Pacific Railway Ltd. (CP)ôs shipments from North Dakota climbed to more than 13,000 carloads last year from about 500 in 2009, Ed Greenberg, a spokesman, said in an e-mail. The Calgary- based company has a similar plan in western Canada.

ñWith an extensive rail network and proven expertise in moving energy, CP offers a flexible option for transporting crude oil and other energy-related products to and from key locations in North America,ò Vice President Tracy Robinson said in an e-mail. ñRail is scalable, allowing CP to effectively keep pace with the shipping needs of producers.ò

Oil Sands

Canadian National Railway Co. (CNR), the biggest Canadian railroad based on annual sales, considers Albertaôs oil sands a chance to expand its business, according to company filings.

ñCN continues to work closely with customers in Alberta to capitalize on oil-and-gas related opportunities,ò the Calgary- based company said. ñCN sees potential for the outbound movement of oil sands products such as bitumen and synthetic crude to refineries in the U.S. Gulf Coast region, or eventually through West Coast ports to offshore markets.ò

Imperial Oil Ltd. (IMO), a Calgary-based unit of Exxon Mobil Corp. (XOM), will consider ñvarious transportation optionsò for oil sands exports, according Pius Rohlheiser, a spokesman.

Cenovus Energy Inc. (CVE) uses railroads to bring in dilutants needed to mix with heavy crude before it can be shipped by pipeline, and to export oil from the Bakken formation in Canada, according to Jessica Wilkinson, a spokeswoman.

Environmentalists' Opposition

Environmental groups such as the Natural Resources Defense Council have campaigned to stop Keystone XL because leaks could threaten drinking water supplies and processing Alberta crude produces more greenhouse gas emissions than conventional oil.

Railroads too present environmental issues. Moving crude on trains produces more global warming gases than a pipeline, the State Department said.

Union Pacific Corp. (UNP), based in Omaha, Nebraska, anticipated an increase in rail traffic with or without Keystone, Chief Executive Officer Jim Young said in an interview.

ñWe would have been involved with moving the pipe and a lot of the construction business in building it,ò Young said. ñOn the other hand, if you donôt build any pipeline capacity, youôre going to be moving a lot of crude by train.ò

It will take five to eight years before oil sands production outstrips existing export capacity, the State Department said.

Tank car utilization is at ñrecord levelsò fueled by demand from oil and natural gas producers, according to Doug Reece, director of marketing for Oakville, Ontario-based Procor Ltd., a rail-car leasing company. The soonest new cars will be available is 2013, he said.

ñIn western Canada, shippers and third parties are investing in the necessary infrastructure and we see strong growth ahead,ò Reece said in an e-mail. ñWe are having regular dialogue with customers about their potential needs, as collaboration and fleet planning have become critical.ò

Rail allows shippers to reach different markets and capture better prices at refineries, said John Mims, a transportation analyst at Friedman Billings Ramsey & Co. in Arlington, Virginia.

ñItôs a good secular growth story for the railroads,ò Mims said in an interview.ñTheyôre playing an increasing role, especially as you see this push back from a regulatory standpoint on the pipelines.ò

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