



Special Report

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Implications of the Gulf Oil Spill

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The BP oil rig explosion that has spewed oil into the Gulf of Mexico since April 20th is the largest environmental disaster in U.S. history. The latest attempt to staunch most of the flow using a containment cap appears promising, but much uncertainty exists, including how much oil will ultimately flow into the Gulf and how many states will be affected. If oil continues to spill at the current rate until August, when relief wells should stop it, the total spillage could be five-times larger than that of Exxon Valdez in 1989. The National Center for Atmospheric Research says the oil could travel along Florida's east coast as far as North Carolina. Weather forecasters are predicting a worse-than-average hurricane season, which could push oil far ashore, magnifying the spill's economic and environmental damage.

Possible impacts of the oil spill include:

Oil Industry

- The President has ordered a moratorium on new deepwater drilling and the suspension of 33 exploration wells already being drilled. More recently, shallow-water drilling in the Gulf was temporarily suspended until companies submit plans to satisfy revised safety and environmental regulations. Clearly, the off-shore oil and gas industry faces tighter restrictions and increased regulation that will reduce earnings. As well, the President is pushing for an end to oil company tax breaks. Royalty payments could rise. Civil liability caps will likely be lifted from \$75 million to possibly \$10 billion. Insurance premiums for offshore oil drillers are set to soar. The costs associated with greater regulation, higher taxes and higher insurance premiums could put upward pressure on oil prices.
- Should the damage and political pressure escalate, the offshore oil industry could languish for years, similar to when the Three Mile Island core meltdown scare in 1979 virtually shut down development in the nuclear power industry. This would give a boost to the alternative energy industry.

Fisheries

- The U.S. government has declared a fisheries disaster in Louisiana, Mississippi and Alabama. Louisiana, reeling after four massive hurricanes in four years, is the closest state to the oil spill and thus the most impacted so far. Its \$2.4 billion seafood industry employs over 27,000 and is the largest private employer in the state. So far, there is no evidence that the oil spill has contaminated seafood in the state, but

precautionary measures have closed one-third of fishing waters in the Gulf, idling hundreds of thousands of commercial fishermen in the region.

- Although fishing continues in the other two-thirds of the Gulf that does not face contamination, demand for seafood could decline given the perceived risks of toxicity. Marine biologists warn of possible devastating consequences to marine life in the Gulf, a region that provides 30% of U.S. shellfish. Little is known about the effects of dispersants (to break up the oil) on marine life. So far, seafood prices have not climbed much in response to the reduced supply in the Gulf, largely because 80% of the seafood consumed in the U.S. is imported, according to the National Fisheries Institute. However, the price of oysters has shot higher, since Louisiana provides nearly 40% of the oysters consumed in the U.S.

Tourism

- Hotel owners and restaurants along the Gulf Coast are seeing cancellations and lost business, offset partially from the number of cleanup workers streaming into the region. Florida's \$60 billion tourism industry, its largest, has lost millions of dollars, according to a tourism official. Tourism employs nearly one million people in the state, which is already suffering from a near-record 12% jobless rate.

U.S. Economy

- Although the environmental damage could be extensive, the impact of the reduction in activity in the Gulf Coast on U.S. GDP will likely be small, and activity associated with the cleanup will offset a portion of the negative impact. This is not to downplay the more significant economic hit confronting Louisiana, Mississippi, Alabama and possibly Florida.
- An escalation of the damage could impede exports and imports, although major shipping channels and ports in the Gulf Coast remain open. The Lower Mississippi ports export over 55% of all U.S. grains inspected for shipment.

U.S. Government

- With the Administration facing voter anger for not resolving the problem sooner, the incumbent Democratic Party could lose seats in the November 2 congressional elections, when all 435 seats in the House and 36 of 100 seats in the Senate are up for grabs. Alternatively, voters seeing the need for even stricter regulation of the oil industry could lean towards the Democrats, especially since Republicans are seen as stronger proponents of off-shore drilling.
- The collateral damage from the oil spill will likely lift the U.S. budget deficit only modestly, as the government will likely force the responsible parties to pay for the costs associated with the cleanup and compensation, a bill that some analysts say could reach \$35 billion.

Canada

- Canadian officials say they have no plans to halt activity at the only deepwater exploration well in North America currently being drilled, which is off the coast of Newfoundland & Labrador, or at three other existing offshore production platforms. As well, the government will continue to grant exploration licences in the Beaufort Sea. However, the government plans to step up regulatory oversight in light of the BP disaster.
- Canadian fisheries could get a boost if consumers shy away from U.S. seafood.
- Alberta's oil sands come out looking "cleaner" in the wake of the Gulf oil spill. This increases the chances that the Obama government will give the green-light to the proposed 2,000 mile underground Keystone Pipeline that would run from Alberta to Texas (a decision is due in the fall), a potential big win for Alberta. Canadian oil sands are already slated to become America's top source of imported oil this year.

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