ECONOMIC VIEWPOINT

Trump's Energy Policy: Why "Drill, Baby, Drill" Is a Pipe Dream

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President Trump wants to strengthen US energy dominance by ramping up oil and gas production. He signed executive orders to simplify the permitting process, open up access to federal lands and remove several regulatory barriers. However, the US market is well supplied, and low oil prices are eroding the viability of new drilling operations. Producers favour profitability and returns to investors, which is hindering potential production growth. In addition, the global market is oversupplied, which is keeping prices down. Measures to deregulate the industry and increase access to federal lands will have a limited impact on production in the short term.

Canada, the largest heavy crude supplier to the United States, may be affected by tariffs, but US refineries depend greatly on this type of oil. Tariffs could increase gasoline prices in the United States and Canada. Although Trump has big plans for the US oil industry, market headwinds and dependence on Canadian oil are limiting the impact of his policies. "Drill, baby, drill" will likely remain a pipe dream.

The New Administration's Goals

President Trump wants to reassert America's energy dominance and keep prices low. He believes his path to achieving this is to "drill, baby, drill" and ramp up domestic oil and gas production. As a result, on his first day in office on January 20, he signed a flurry of memoranda and executive orders, including *Unleashing American Energy* and *Declaring a National Energy Emergency* (box on page 2), dismantling a number of mostly environmental regulations that he believes are holding back production.

However, it's worth noting that outside of the Oval Office's rhetoric, the United States isn't suffering from an energy crisis like Europe did in 2022 when war broke out in Ukraine. The US market is well supplied, and there are no serious issues related to fossil fuel production and consumption in the coming years.

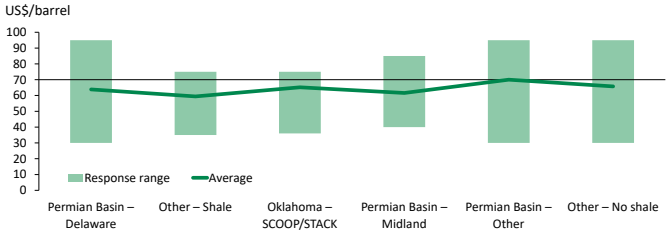
But the Market Isn't on the Same Page

Since oil prices collapsed in 2014–2015, US producers have focused on profitability and providing strong returns to investors. Current price levels, which are below the break-even point for some wells (graph 1), could curb the potential for increased US production. On top of that, US commercial oil inventories are high, which also isn't conducive to increasing supply. Oil companies plan their investments over a 10- to 30-year period, depending on the type of installation. So they have to price in the risk that the next US administration may have completely different objectives.

Graph 1

Some US Oil Producers Have a Breakeven Point Above US$70 per Barrel

Breakeven points for new US oil wells*



* Survey of US oil producers by the Federal Reserve Bank of Dallas, Q1 2024 (137 respondents).

Federal Reserve Bank of Dallas and Desjardins Economic Studies

We're already in a global oil glut, and the International Energy Agency is forecasting a surplus of 0.7 million barrels per day (MMb/d) in 2025 (graph 2 on page 2). As we already discussed in a previous Economic Viewpoint, this puts oil prices at risk of a major correction. It's also worth noting that OPEC+ has record unused production capacity that could flood the market. As a result, the price of West Texas Intermediate (WTI)

Box
Executive Orders Signed by Donald Trump

Unleashing American Energy

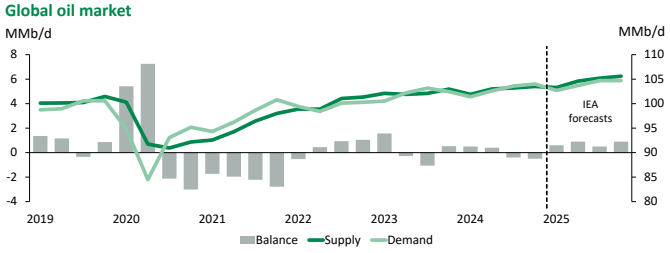
- Potentially pauses the disbursement of funds appropriated through the *Inflation Reduction Act or the Infrastructure Investment and Jobs Act*. This doesn't completely remove funding under these two acts, but it does aim to put an end to federal assistance for electric vehicles, and solar and wind energy.
- Expedites and simplifies the permitting process to improve the competitiveness of American businesses and make obtaining permits easier.
- Increases access to certain federal lands for oil and natural gas production.

Declaring a National Energy Emergency

- Gives the government additional powers to expedite permitting, modify existing regulations, allocate additional funds, and order emergency studies (first step for larger changes).

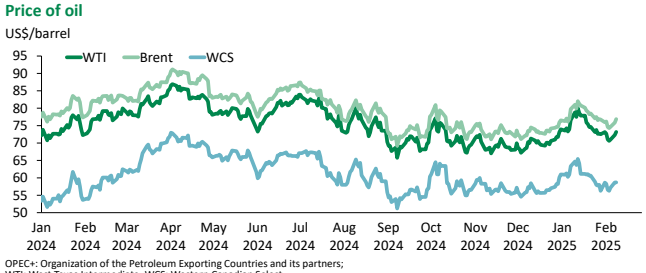
has fallen by more than 12% from its July 2024 peak, and any rebounds since have been short-lived (graph 3). We expect prices to continue to fall. Our year-end target for 2025 is US$68 per barrel. The question now is where any additional oil produced would end up.

Graph 2
A Market Glut Is Expected in 2025



MMb/d: Million barrels per day
International Energy Agency (IEA) and Desjardins Economic Studies

Graph 3
Oil Prices Are Falling as Supply Increases



OPEC+: Organization of the Petroleum Exporting Countries and its partners;
WTI: West Texas Intermediate; WCS: Western Canadian Select
Datastream, Bloomberg and Desjardins Economic Studies

How Would Trump's Energy Policy Impact the Oil Sector?

The measures announced can be divided into two categories: Deregulation and access to federal lands for drilling. How could these policies impact US crude oil production?

Deregulation

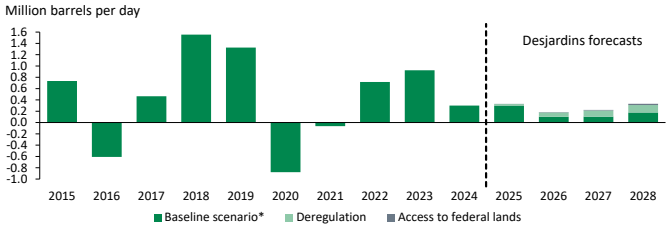
The Trump administration announced the removal of significant regulatory—primarily environmental—barriers, which is likely to bring down production costs. However, it's difficult to assess the concrete impact of these policies on oil prices. Estimates vary widely, especially by political affiliation, but generally land at between 0.5% and 5% of total production costs. Importantly, some producers may maintain their environmental practices, especially when it comes to previous investments in equipment, so the impact on costs could be minimal.

To keep things simple, we've assumed that the announced policies will reduce production costs by 2.5%. Our analysis shows that supply would likely be little changed in 2025 and 2026 (graph 4 on page 3). However, after three years the effect ramps up, bringing an additional 0.1 MMb/d to market per year. That said, we're still a long way from the production gains seen during the shale oil boom between approximately 2004 and 2014.

Graph 4

Trump's Policies Will Likely Only Have a Marginal Impact on Oil Production

Growth in US crude oil production



* U.S. Energy Information Administration baseline scenario

U.S. Energy Information Administration, U.S. Department of the Interior and Desjardins Economic Studies

Access to federal lands

The Biden administration had limited federal leasing for drilling, but Trump reversed this decision on January 20. In 2023, a record low of just 91,712 new acres were leased, so we're assuming that new drilling leases will increase by just under 1,300% by 2028, bringing them close to the levels we saw during Trump's first term (graph 5 on page 4). However, the impact on US crude production will likely be minimal, with an additional gain of just 0.04 MMb/d four years after Trump's executive order, as only 15% of US production came from onshore federal lands in 2023 (graph 6 on page 4).

Low prices hurt

In both cases, lower prices weaken the impact of additional production gains. For illustrative purposes, we have broadened our price assumptions to consider three other scenarios. Under the WTI at US$60/barrel and US$50/barrel hypotheses, the increase in supply from deregulation and greater access to federal lands is completely offset by lower oil prices (table). The price of oil is still the variable with the biggest impact on production. As a result, in the US$85/barrel WTI scenario, US supply could be 0.8 MMb/d higher than the baseline scenario in 2028.

Where Does Canada Fit In?

Canadian oil is used primarily as an input for US production of petroleum products such as gasoline and diesel. In fact, 70% of the crude oil used by US refiners in PADD 2[1] comes from Canada (graph 7 on page 4). That's followed by PADD 4, where Canadian oil is used in 45% of petroleum product production. Canada accounts for 60% of total US crude oil imports. Plus, refinery output from PADD 2 and 4 is primarily used by US consumers. Respectively, only 15% and 0.6% of petroleum

TABLE

Impact of Donald Trump's Energy Policy on US Production

Million barrels per day	2022	2023	2024	2025	2026	2027	2028
Baseline scenario*	11.99	12.9	13.2	13.5	13.6	13.7	13.9
Growth		*0.91*	*0.3*	*0.3*	*0.1*	*0.1*	*0.2*
Scenarios (deviation from baseline scenario)							
WTI price = Dec. 2024 Economic and Financial Outlook				**0.03**	**0.09**	**0.13**	**0.17**
Impact of federal land leasing				0.00	0.01	0.02	0.04
Impact of deregulation				0.03	0.08	0.11	0.13
WTI price = US$60/barrel				**-0.28**	**-0.44**	**-0.51**	**-0.55**
Impact of federal land leasing				0.00	0.00	0.01	0.02
Impact of deregulation				-0.28	-0.44	-0.52	-0.58
WTI price = US$50/barrel				**-0.60**	**-1.06**	**-1.28**	**-1.44**
Impact of federal land leasing				0.00	-0.01	-0.01	-0.01
Impact of deregulation				-0.60	-1.04	-1.27	-1.43
WTI price = US$85/barrel				**0.24**	**0.56**	**0.74**	**0.89**
Impact of federal land leasing				0.01	0.03	0.04	0.08
Impact of deregulation				0.23	0.53	0.70	0.81

* U.S. Energy Information Administration baseline scenario.

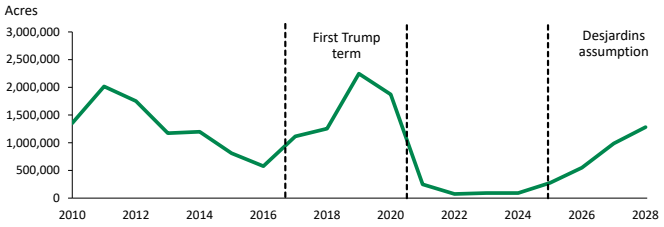
U.S. Energy Information Administration and Desjardins Economic Studies

[1] Petroleum Administration for Defense Districts are geographic aggregations of the 50 US States and the District of Columbia into five districts, used for energy management purposes.

Graph 5

Trump's Policies Are Likely to Significantly Increase Leasing of Federal Lands for Oil Production

Federal land leased for oil drilling

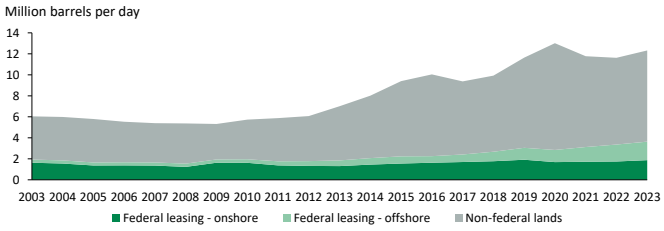


U.S. Department of the Interior and Desjardins Economic Studies

Graph 6

Federal Lands Account for 29% of Total Crude Oil Production

Gross crude oil production by land type

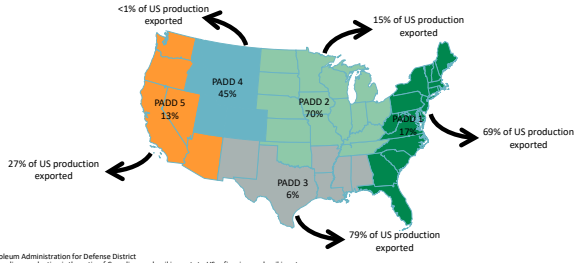


U.S. Energy Information Administration, U.S. Department of the Interior and Desjardins Economic Studies

Graph 7

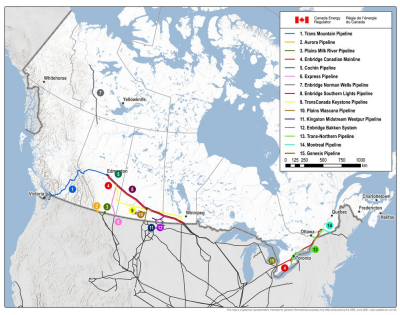
Canadian Oil Is Used Primarily as an Input for Gasoline Production for US Consumers

Share of Canadian crude oil in US refinery input



PADD: Petroleum Administration for Defense District
Share of Canadian production is the ratio of Canadian crude oil imports to US refineries crude oil input.
Share of production exported is the ratio of US petroleum product exports to petroleum product production
U.S. Energy Information Administration and Desjardins Economic Studies

Graph 8



Canada Energy Regulator and Desjardins Economic Studies

products produced in these regions are exported. Therefore, tariffs on Canadian oil would hurt US households and work against Trump's goal of lowering energy prices.

Americans Have Few Alternatives

The United States has one of the most developed and complex petrochemical industries in the world. However, it's dependent on heavy crude. Before the shale boom, when light crude[2] was scarcer, the United States invested massively in its refineries to be able to process the more abundant heavy crude and guarantee its energy independence. Canadian production, which is approximately 50% heavy crude, became the main supply source for US refiners. These refiners would suffer a significant loss of productivity without this supply. Put simply, US facilities are set up to process heavy crude.

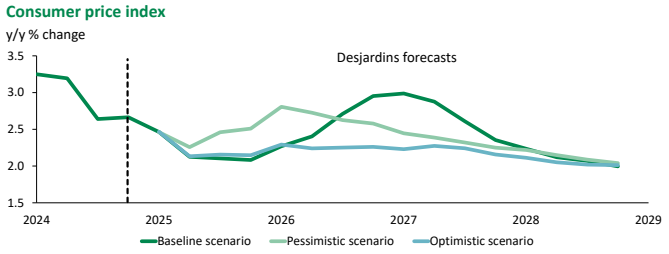
If tariffs are imposed on Canadian oil, the United States has three options. Refineries could diversify their supply, either by expanding into other countries like Venezuela or producing it locally. However, this could be a logistical nightmare given that the US transportation infrastructure—especially in PADD 2 and 4—is configured to import Canadian oil through an extensive pipeline network (graph 8). It's also much more profitable for US oil companies to produce light crude, which has a higher market value.

The second option would be for refineries to invest in converting their facilities to process light crude. Since the shale revolution, most US production has been light crude, which is also expected to be the main source of growth over the next few years. To make this option viable, refineries would need some guarantee that the tariffs will be applied for the long term—or even permanently—to justify the millions of dollars needed to convert their facilities.

Lastly, refiners could simply absorb the tariffs and produce at a higher cost. This is probably the most plausible option in the short term, especially if tariffs are only temporary. Refiners would also likely diversify their supply sources slightly, which would erode productivity. As mentioned in our recent Economic Viewpoint, the impact of tariffs could fuel inflationary pressure in the United States (graph 9 on page 5). Pump prices would be particularly affected and could increase by about 5% on average if a 10% tariff is imposed on Canadian crude. Some areas—especially in the Midwest—may see larger spikes.

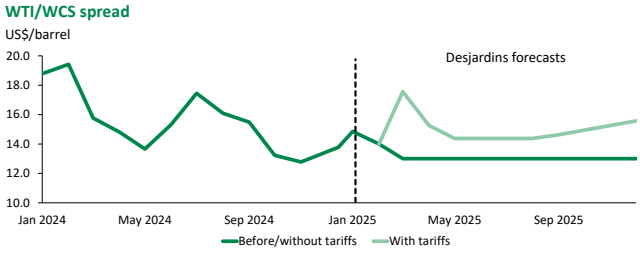
[2] Different types of crude oil exist and are defined based on a scale of API gravity. Light crudes generally exceed 38 degrees API, and heavy crudes are commonly labelled as all crudes with an API gravity of 22 degrees or below.

Graph 9
Tariffs Would Drive Up Inflation in the United States



Bureau of Labor Statistics and Desjardins Economic Studies

Graph 11
There's No Alternative to Canadian Oil in the Very Short Term

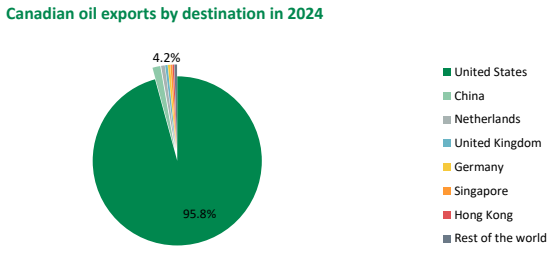


WTI: West Texas Intermediate; WCS: Western Canadian Select
Bloomberg and Desjardins Economic Studies

Impact on Canada

Canada also has few options since it exports 96% of its crude oil to the United States. It wasn't until the Trans Mountain Expansion pipeline opened in early 2024 that Canada had a genuine export path to the Asian market. And the volumes that head to Asia are still very low compared to what our neighbour to the south imports (graph 10). However, additional growth in US production isn't a major issue for Canadian producers. As mentioned, not all oil is equal, and Canadian heavy crude is expected to remain a fixture at US refineries for a long time, even though production of light crude is increasing. However, overproduction could send oil prices lower.

Graph 10
Almost All Canadian Oil Exports Go to the United States



Statistics Canada and Desjardins Economic Studies

Tariffs could widen the spread between WTI and Western Canadian Select (WCS) by around US$2 per barrel on average in 2025 (graph 11). This spread may widen further in the first few weeks as US refiners draw from their own inventories rather than importing Canadian oil. However, the Americans will soon be faced with the reality that they depend on our heavy crude, which would narrow the spread. That said, if tariffs remain in place for the long term, refiners may gradually reduce their imports from Canada. Canadian producers could see their profit margins decline, especially for light crude. But tariffs on energy are painful for everyone. The United States relies on Canadian oil just as much as Canada depends on US refiners.

Although Canada produces more gasoline than it consumes, some regions rely on imports, 60% of which come from the United States. Therefore, prices at the pump would probably also rise in Canada. We estimate that a 10% tariff combined with the depreciation of the Canadian dollar could push average gas prices in Canada up by 1% to 2% in 2025. That said, refineries in eastern Canada could see their exports to the United States fall, triggering a gasoline surplus in the region. In this case, we could see lower prices at the pump in some provinces, including Quebec. However, these cheaper prices likely wouldn't stay around for long, because refiners would adjust their production levels.

Conclusion

Although Donald Trump has big plans for the US oil industry, he can't escape the prevailing market headwinds. Our analysis shows that greater access to federal land for drilling would only increase US crude oil production very slightly. Deregulation could boost anticipated growth, particularly after three years, but won't come close to the gains we saw during the shale revolution.

Since the United States depends on heavy crude to produce gasoline at its refineries, tariffs would push up prices at the pump, which would be inconsistent with the new administration's goals. US oil companies have also said they're opposed to tariffs on Canadian crude, and some disagree with aspects of the administration's climate policies. There's still a lot we don't know about President Trump's tariffs and energy policy, but it seems clear that "drill, baby, drill" will remain a pipe dream.