"Access to oil resources" for IOC’s : How OPEC countries can react?

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If in the short term, prices will fluctuate probably around 55 $/bbl, what about the longer term? With a relatively rigorous demand growth, the balance on the market will be strongly influenced by OPEC countries ability to produce more. Presently, the main share of OPEC production is under the responsibility of the NOC’s. What could be the contribution of IOC’s is increasing that production in the future?

Actually, “Access to oil resources” in producing countries is being one of the main worries for large importing countries and international companies.

This expression, more and more frequently used in the oil industry, refers to foreign operators’ rights and conditions to access and exploit oil and gas reserves in producing countries. But this sibylline phrase also suggests the existence of artificial barriers and bitter competition between interested parties. The problem is so great that, for some, this liberty of access will depend, in large measure, on whether or not a global energy crisis develops.

Worries about oil shortage and “access to resources”.

Faced with the well-established facts of limited supply versus expanding demand, there is a growing sentiment that oil is becoming progressively more scarce. Specialy with the appearance of some warning signals which confirm that we are facing a turning point in the global supply-Demand balance : very limited non-Opec oil supply, minimal spare capacity in Opec countries, commercial inventories at operational minimums and increasing volatility of the oil markets.

Worries are so high that the growth of energy consumption in emerging economies, most notably China and India, has become problematic for some. One practically reproaches them for wanting to catch up with industrialised countries, yet their consumption per capita is one-tenth that in rich countries. However, we all know that it will therefore be difficult to dissuade them from consuming more oil. In fact, even if high prices “destroy” part of demand, particularly in poor countries, the global increase in oil consumption is unavoidable

From an another side, the persistence of geopolitical tensions in some important production areas such Middle East, Africa, Venezuela, around Caspian Sea, increases the risks of a failure of one main source of supply.

The criteria of holding reserves becomes very important. And the validity of their estimates a very sensitive issue. We remember, in the very recent past, the price impact of an US energy-market investment banker, Mr Simmons, contesting Saudi Arabia’s production capacity and reserves estimates, or the dimensions of the scandal after Shell was caught “cheating” in its reserves statements. More and more frequently, companies are adding
reserves more slowly than production depletes them, and – seeing companies liquidating their reserves feeds bullish market sentiment.

**Race to guaranty supply sources.**

In such atmosphere, how much will be tough the race to guarantee supply sources?

We know that the peril – in terms of resources – is not for tomorrow. The majors, OPEC and the International Energy Agency (IEA) consider that currently-proved reserves – not to mention those yet to be discovered – are sufficient to cover several decades. For them, the problem for the years coming, is the risk of delays in getting the required production infrastructures.

Consequently, it is a logical option for consuming countries to try to position themselves, the nearest as possible, in upstream natural gas and oil.

President George W. Bush repeats incessantly that oil issues relate to the “vital interests” of the United States. European Union Countries seem worry about their long term supply. China and India are acting as never in the past to conclude contracts with exporting countries.

Japan, China, India and the US are competing to assure diversified supply by taking upstream positions in Russia and Caspian Sea countries. For big importers, the best option seems to send their companies to the sources of production to confort guaranties for the supply.

Some take the position that only the majors can assure freely-flowing supply – and that, only if they are left free to act. Of course, it would be ideal (for the majors) if conditions (in producing countries) were equivalent to those to which they are accustomed in the North Sea and US Gulf of Mexico, that is to say under strict market’s rules. This is unrealistic: globalisation has not yet proceeded that far. IOC’s will be easily pleased with less.

**The renewal of “oil nationalism”.**

But where are producing countries in all of this ? High prices were supposed to encourage them to increase production and eventually to change their legislation to attract foreign companies. For the moment, with the exception of rare cases such as Algeria, we see the opposite. Large producers such as Saudi Arabia, Mexico, Iran and Kuwait still do not wish to open the upstream, preferring to reserve that domain exclusively for their national companies.

Other large producers such as Russia, Kazakhstan, and Venezuela which opened considerably a few years ago, are taking advantage of the increase in their revenues to tighten the conditions of already-signed contracts, reinforcing the role of their national companies and increasing the taxes on exports.

Not to mention Bolivia and Ecuador where, after popular movements contesting the manner in which oil “rents” are shared, they evoke the possibility of nationalisation!
Commentators describe this evolution in pejorative terms, calling it “the renewal of oil nationalism”.

But in a context where even Washington refuses – in the name of protecting its national interests – to let China’s CNOOC purchase oil-giant Unocal, and other rich countries cite “economic patriotism”, we should prepare to live with this “oil nationalism” from producing countries for some time to come.

**New competitors.**

The other striking fact is the growing role of new competitors who do not hesitate to sweeten their bids in order to gain exploration contracts, as was recently the case in Libya. Remember that, up until now, the majors refer to a price of $20-25/b to calculate profitability, even while prices are cruising above $60. Among these new actors are the national oil companies of large emerging economics (China, India and Brazil), State owned companies of exporting countries such as Malaysia’s Petronas, Algeria’s Sonatrach or Kuwait’s KPC and even independent companies from Persian-Gulf countries.

All this does not make the majors’ task easier.

We are far from the time when oil-producing countries behaved as rivals, multiplying the concessions they granted in order to attract foreign companies with high return expectations for their investments. The arrival of new competitors, wanting access to reserves, has changed the game. And I suspect Producing countries trying to profit from that new rapport de forces.

**For Producing countries the “fair price” could become not just that of a barrel of oil.**

Has the primary importance of the majors been called into question? Definitely, no. Their discretion should not make us forget their power, reinforced by the 1990’s mega-mergers. The turnover for one year of Exxon alone practically equal the export revenues of all OPEC countries combined.

However, even if the majors’ know-how is unequalled in terms of reservoir engineering and production in extreme conditions, so indispensable for the future, they should probably re-think their strategies.

Although their adversaries have as yet gained only a modest share of the new contracts granted, it is sufficient to change the rules of the game because it permits exporting countries continue to reinforce the role of their national operators and to try to take advantage of competition to obtain better terms. They might even, in a new paradigm, no longer focus on the strictly-fiscal aspect and take the present oil context to negotiate other issues.

I expect that they could in the future ask for more counter-parties to the long-desired opening of their upstream. Oil being vital to the global economy, their responsibility should, certainly, be engaged. But one could understand also that is legitimate for them to claim a fair price.
By price, I do not mean simply that of a barrel, but a radical change of the nature of relations between international companies and those of producing countries, a development of real partnerships with inter-locking interests, such as the opening of the upstream sector in exchange for assets in downstream located in importing countries, that is to say, where also a part of the profits in oil and gas supply chains are made.

**IOC’s/OPEC countries relations in the near future (2 - 3 years)**

- **Saudi Arabia**: Oil upstream is a strategic asset for the Saudi government, a card for negotiation. I don’t see a big change in the near future. 12.5 to 15 Mbd in 2010: is that enough?
- **Iraq**: Not yet to morrow having IOC’s developing big fields. New oil legislation and security conditions needed.
- **Iran**: after long debate inside national direction some adaptation to the legislation but not yet for US companies.
- **Kuwait**: They will adopt the law for “Kuwait project” but the impact comparing to the present forecasts of production capacity will not be substantial.
- **Arab Emirates**: increase of production forecasted but no big project.
- **Qatar**: very opened for IOC’s but limited oil production development and more gas-oriented projects.
- **Nigeria**: nearly more than 4 Mbd with IOC’s participation but with tougher conditions.
- **Algeria**: good legislation for IOC’s but relatively modest oil prospects.
- **Libya**: opening politically negotiated.