Egypt Enjoys Unexpected Bid Round Success

By improving the fiscal terms, Egypt has managed to secure significant investment into its upstream, even as producers are still owed billions by the government.

Egypt's latest auction of oil and gas blocks is crystallizing into the envy of its neighbors, as international oil companies (IOCs) flock to Egyptian acreage, while upstream investment into other key North African producers stagnates.

This week, IOCs picked up further blocks in Egypt, offered in a bid round launched in the final days of 2013, when the country was embroiled in political turmoil and economic difficulties. France's Total, BP and the UAE's Dana Gas were the latest companies to sign up to exploration licenses, encouraged by gas price reform, improving state finances and political stability.

"The bid round results indicate confidence in the Egyptian upstream gas sector," says Justin Dargin, Middle East Energy Expert at the University of Oxford, who adds that the strong interest is "fundamentally a pricing issue."

Key to the appeal of Egypt's acreage is a revision of a pricing policy that had restricted remuneration for gas production to a miserly $2.65/mn BTU. Onshore producers in areas with dense existing gas infrastructure – such as the Nile Delta – have been able to turn a profit, especially if the gas is 'wet,' and contains a significant cut of (more profitable) liquids. But with offshore drilling costs rising, it has not proved sufficient to incentivize offshore drilling, particularly in deepwater acreage.

Minister of Petroleum Sharif Isma'il last year pledged to raise the prices paid to producers to accommodate for higher development costs, a change that increased the interest in offshore projects in particular. Egypt had already relaxed its rigid pricing formula for the 1bn cfd WND project, with BP and RWE reportedly set to receive $4.20/mn BTU.

MORE BLOCKS AWARDED

On 29 September Dana Gas announced it had been granted exploration rights to the North El Salhiya and El Matariya onshore gas blocks in the Nile Delta (see map and table). The concessions lie next to Dana's El Manzala, West El Manzala and West El Qantara blocks . BP is the operator at El Matariya with a 50% stake in the block, and will bear the costs of the first exploration well. It then has the option of farming into the Oligocene layers of Dana's existing development leases with a 50% stake as well as taking a 50% stake in the Oligocene geology of North El Salhiya, should drilling there prove a success.

France's Total has meanwhile been awarded the neighboring Nile Delta block of North El Mahala. The deal marks a step up in Total's commitment to Egypt's upstream. The company's sole existing Egyptian upstream, the offshore East El Burullus block, was due to expire this year, and with Total reporting that an initial late-2013 exploration well had "disappointing results" it is unclear if the permit has been renewed.

This week's deals add to a string of oil and gas blocks already granted to international bidders.

Eni a week earlier announced the award of three licenses by the Egyptian government, as the Italian company added the North Leil and the Karawan to its existing Shorouk block in the Mediterranean, creating a massive deep offshore gas exploration area (see map). Eni also signed up for the on-

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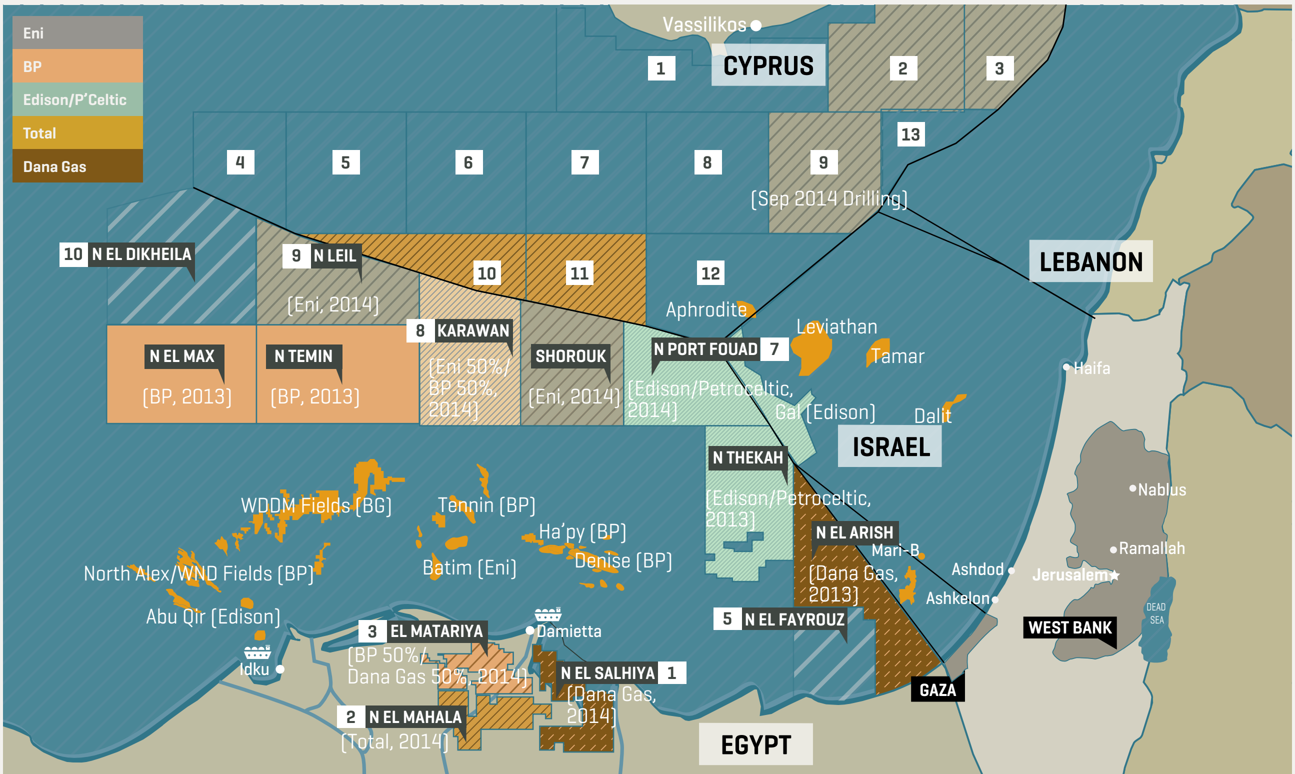
EGAS 2013/2014 BLOCK AWARDS*

GAS FIELDS



*2014 BLOCKS ARE NUMBERED (SEE TABLE). BLOCKS 5 AND 10 ARE NOT YET AWARDED. SOURCE EGAS, MEES.

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shore South West Melehia oil block.

BP holds a 50% share in the Karawan block, extending its sizeable project pipeline in Egypt. The UK major is the operator of the 1.8 tcf West Nile Delta (WND) development, which it aims to bring online with its minority partner RWE by 2017, and is active drilling in other offshore acreage.

In addition to Eni, compatriot Edison also now holds three contiguous East Mediterranean deepwater exploration blocks. The Italian firm signed up for the North Port Fuad block with Irish independent Petroceltic in the latest bid round. This abuts Eni's deep offshore acreage. The same two partners took the neighboring North Thekah block last year after EGAS' previous bidround. This acreage complements the Gal exploration permit that Edison holds on the Israeli side of the two countries' maritime frontier.

Awards of onshore blocks offered by EGPC in a bid round contemporaneous with its gas-focused affiliate EGAS have been less numerous. Edison will partner Germany's RWE-Dea on the oil-prone East Ras Fanar and Northwest El Amal blocks in the Gulf of Suez, adding to existing RWE-Dea acreage in the area.

Reuters reports that Tunisia's HBSI also won exploration rights to a block, but does not name the acreage. According to an Egyptian government press release US independent Apache was awarded two blocks in the Western Desert, which has not been confirmed by the company.

CONTRASTING FORTUNES

Egypt's successful bid round stands in stark contrast to Algeria, where the government has only managed to find takers for four of the 31 blocks it had put on offer this week. In Libya, three years of political chaos has left the IOCs eying the exit door, and a new bid round is a distant prospect at best.

Apart from adapting its prices, Egypt also appears to have overcome the political volatility the aftermath of the Arab Spring in 2011. The protests following the ouster of President Muhammad Mursi and his Muslim Brotherhood government by the army last year were quickly suppressed, and this June's election of military strongman 'Abd al-Fattah al-Sisi as president went smoothly. The return of army rule led to an inflow of economic aid from the Gulf, which has stabilized the economy and set it on a path to growth.

Energy companies will be further encouraged by a reduction in domestic subsidies on natural gas and transport fuels, which had been crippling the government's finances and impeding its ability to pay producers. Mr Sisi became the first head of state in the Middle East to push through the politically difficult move soon after the election. Apart from swelling state coffers, it will also help reduce domestic demand for gas, which is already outstripping production, so taking some pressure off the upstream sector to deliver on the bid round.

"It's going to take years for some of these fields to be up and running. On a positive note though, the upward pressure on domestic energy prices will reduce consumption," said Mr Dargin. Any shortfalls in supply will likely be made up by LNG imports, which the government is currently negotiating, albeit without much success.◆◆

EGAS: BLOCKS OFFERED IN 2013-14 BID ROUND*

					Previous Exploration		
Block Name	#	Winner	Location	sq km	Wells (#, last)		Prev. Operator**
N El Salhiya	1	Dana Gas	Onshore E Nile Delta	1,527	11	2012	Dana Gas
N El Mahala	2	Total	Onshore E Nile Delta	1,028	55	2010	Centurion
El Matariya	3	BP 50%op, Dana Gas 50%	Onshore E Nile Delta	960	12	2010	Dana Gas, P'Celtic
N El Fayrouz	5		Offshore North Sinai	2,280	9	2011	Tharwa
N Port Fuad	7	Edison 50%op, P'celtic 50%	Offshore Med	3,397	-	none	Shell
Karawan	8	Eni 50%, BP 50%	Offshore Med	4,565	1	2000	Shell
N Leil	9	Eni	Offshore Med	5,105	1	2007	Shell
N El Dikheila	10		Offshore Med	7,150	3	2007	Shell

*TOTAL 8 BLOCKS (NO BLOCK 4 OR 6). **MOST RECENT. SOURCE: EGAS

PAYMENT PROBLEMS, AND SOLUTIONS

The success of Egypt's latest bid round is all the more remarkable as producers are owed billions in outstanding receivables. In the aftermath of the Arab Spring, payments to IOCs slowed; companies were owed at least $7.5bn by the government as of end-July. Egypt paid out $1.5bn in outstanding debt in December 2013 but despite this its debt pile grew by $1.4bn in the first half of 2014. LNG exporters BG Group and Eni-led Union Fenosa have seen their profitability in Egypt collapse as the government forced them to divert their gas output to the domestic market.

However, according to the oil ministry, Egypt on 2 October paid down a second $1.5bn tranche of its debts to IOCs.

According to the Egyptian oil ministry's calculations, with the latest $1.5bn in payments the balance owed to IOCs falls to $4.9bn (implying $6.4bn immediately prior to the latest payments). Egypt's calculations of receivables have consistently been lower than those given by the companies; seemingly the result of Egypt adopting a more relaxed definition of "overdue".

Oil Minister Sharif Isma'il, in the ministry's 2 October statement, says that by reducing the debt to the IOCs, the government aims to provide them with incentives to accelerate exploration and ultimately increase future oil and gas production. This in turn will help cut Egypt's current dependence on imported oil products, he says, highlighting the potential for a virtuous circle whereby a lower oil import bill will create the necessary conditions for the regular settlement of Egypt's dues to IOCs.

The latest $1.5bn payment comes after Egypt secured an E£10bn ($1.4bn) syndicated loan from a consortium Egyptian, lead managed by National Bank of Egypt, and with the participation of Commercial International Bank, Arab African International Bank, Banque Misr, and QNB Alahli (majority owned by Qatar National Bank).

The loan is made up of two tranches: $550mn is repayable in four years including one year grace period, and E£6.040bn ($844mn) repayable in five years repayable in five years including a one year grace period. It was signed with two wholly-owned subsidiaries of the Egyptian General Petroleum Corporation (EGPC), Misr Petroleum Company and Petroleum Cooperative Society.

In a related development, a source at the Ministry of Finance confirms that Egypt this month plans to repay Qatar $500mn, part of a bank deposit placed with the Central Bank of Egypt during the short-lived term of ousted Qatar-backed Islamist President Muhammad Mursi. This is to be followed by a further amount of $1.5bn in November.

Producers in Egypt are increasingly looking to creative solutions to increase revenue streams.

Dana Gas this week announced an agreement with the government to sell condensate from its gas fields to the international market. The proceeds will reduce the company's receivables of $280m to "nominal levels" by 2018, the company says. The arrangement forms the basis for a seven year investment program that will raise production by 160mn cfd and 5,600 b/d of condensate by 2017. Dana plans to drill 37 new wells and do work over at an equivalent number of existing wells. The investment drive will result in 8-9mn barrels of additional condensate, says the firm.

Italy's Edison has come to a similar agreement with the government, and is selling condensate it produces at its 250mn cfd Abu Qir gas field as well as additional condensate supplied by state-owned EGPC, the firm told MEES in June (MEES, 6 June).

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