Natural Gas Daily

interfax

www.interfaxenergy.com
Volume 3 Issue 60
Tuesday, 26 March 2013

Gulf sour gas: a sweeter prospect for IOCs

The ADCO licence and fields, which produce about 1.4 million barrels of oil per day.

Leigh Elston Middle East & Africa editor

THE world's largest oil companies showed little interest in a contract to develop Abu Dhabi's Bab sour gas field when it was first tendered in 2007, but attitudes have changed dramatically since then.

With the Bab re-tendering process drawing to a close, fierce competition to secure the $10 billion deal shows not only that complex domestic gas projects in the Gulf are now considered profitable for IOCs, but that they are also of growing strategic and political importance for foreign governments and other businesses in the region.

"Western governments and their respective IOCs are viewing the Gulf in a different light," said Justin Dargin, a Gulf gas specialist at the University of Oxford's School of Environment and Geography and president of Global Core Energy.

"They're taking these contracts seriously because they think they will be a toe-hold for their national companies to expand in the region – and not just for other energy deals, but for potential arms contracts, construction deals and overall trade and bilateral investment," Dargin added.

Total, BP, Shell and ExxonMobil are keen to protect and expand their oil and gas interests in Abu Dhabi, backed by strong political support from home. French President François Hollande, UK Prime Minister David Cameron and the United States Secretary of State John Kerry have all visited Abu Dhabi within the past five months and are likely to have promoted the interests of their respective IOCs.

Winning the Bab deal is strategically important for operators in Abu Dhabi as it could improve their chances of remaining in the United Arab Emirate's largest onshore oil concession, ADCO – in which the Bab field lies – when the contract expires in January 2014.

The ADCO licence – held by state-owned Abu Dhabi National Oil Co. (ADNOC: 60%), Total (9.5%), BP (9.5%), Shell (9.5%) and Exxon (9.5%) – includes the onshore Asab, Bab, Bu Hasa, Sahil and Shah fields, and produces around 1.4 million barrels of oil per day.

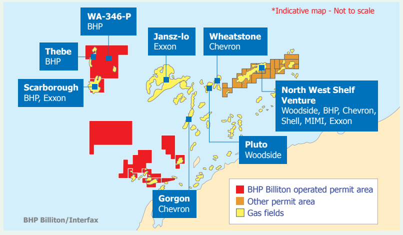
Shell takes the lead

Total and Shell are the front-runners for the Bab project. Both companies are 15% shareholders in Abu Dhabi Gas Industries, which operates the gas infrastructure and processing plants around the Bab field.

Although Total was rumoured to be the favourite to win the project when it was first tendered in 2007, it now

➤ 02

Inside Natural Gas Daily



LNG
Aussie ministers argue over FLNG merits
Page 5

Policy & Regulation
Risks and rewards for stricter US LNG export rules
Page 9

Plus...
US LNG deal looks good for Centrica – analysts 3
Russian ministry backs Gazprom against Rosneft 4
Turkmenistan exports 50 bcm of gas to China since 2009 6
China Number Crunch 7
Peru returns to bid round fray this year 10

NGD holiday schedule

Natural Gas Daily will take a break over the Easter holidays and publish its final issue for this week on Thursday, 28 March. Publication will resume on Tuesday, 2 April 2013.

➤ 01 appears the French oil major has been sidelined in favour of Shell. ADNOC recommended Shell as developer of the project to the Supreme Petroleum Council (SPC), industry sources told *International Oil Daily* last week.

Although the SPC Abu Dhabi's Executive Council usually follows ADNOC's recommendations, it has yet to award the contract, and Total's significant experience developing sour gas in France and the North Sea may help it clinch the deal.

> Producing sour gas in the UAE and the rest of the GCC is not a commercially viable venture, on the basis of selling the gas at the fixed price of around $1/MMBtu, when it costs upwards of $5 to produce.
>
> **JIM KRANE**
> Gulf energy analyst, Cambridge University

"France, as with China, does not involve itself in the domestic affairs of many countries with which it conducts business," said Dargin. The UK, in contrast, has criticised the UAE for its crackdown on Islamist extremist groups and other human rights issues, which reportedly led to BP's exclusion from the pre-qualification list for the ADCO oil concession renewal last year.

While BP is now back in the running for the concession, the earlier blacklisting highlighted the pivotal role diplomatic relations play in promoting big business interests in the Gulf.

A sign of things to come

The Bab project, which has a hydrogen sulphate content of around 28%, is an expensive, complex and potentially dangerous field to develop. It is in a sensitive area, "more or less at the heart of Abu Dhabi's oil production. Therefore, there are some serious health and safety concerns", said Dargin.

In the past, low gas prices in the UAE have deterred IOCs from investing in such large and complex gas projects; ConocoPhillips pulled out of the Shah sour gas development in late 2010 because of the poor economics. However, the project forms a vital component of Abu Dhabi's strategy to bring at least 56.64 million cubic metres per day of non-associated gas production online over the next few years to feed the emirate's soaring electricity demand.

There is an acceptance among policymakers that, as the emirate starts developing more non-associated gas reserves and importing LNG, it can no longer rely on the prevailing $1.30/MMBtu price structure that covers the cost of producing and transporting associated gas.

"Producing sour gas in the UAE and the rest of the Gulf Cooperation Council is not a commercially viable venture, on the basis of selling the gas at the fixed price of around $1/MMBtu, when it costs upwards of $5 to produce," Jim Krane, a Gulf energy analyst at Cambridge University's Judge Business School, told *Interfax*.

While the Arab Spring has put a dampener on reform, Krane's research shows there is still a drive to raise prices and reduce subsidies. "My surveys of UAE policymakers find that most see domestic consumption as an economic threat to oil exports – the country's biggest line of business," he said.

However, the UAE is unlikely to have any substantive gas pricing reform in place by 2014 when the Shah project – now under development by US company Occidental Petroleum – is expected to come online. It is, instead, developing innovative pricing formulas with IOCs to make non-associated gas development attractive.

"An IOC that will produce from a technically challenging field will be offered a pre-determined gas price for extraction, as well as access to NGLs and condensates. In the aggregate, this structure would, at a minimum, meet the cost of production and provide an additional return on investment," said Dargin.

Investors are likely to be playing the long game. The UAE is a large – and rapidly expanding – gas market, and growing confidence in the inevitability of gas pricing reform means IOCs want to secure a stronghold in the region now.

"All across the Gulf, governments are experimenting with price reform at the margins," said Dargin. "However, Oman confronted the issue directly and recently doubled the domestic gas price – the first time a country in the Gulf has done so – in order to meet the cost of production at the Khazzan and Makarem tight gas fields. In North Africa, Egypt is also experimenting with price reforms. Difficulties in producing from non-associated gas fields are now pushing countries in the MENA region to make difficult choices." ■

Contact Leigh at leigh.elston@interfax.co.uk

Today on interfaxenergy.com

Gas to Power

Coal strikes back in US power price war

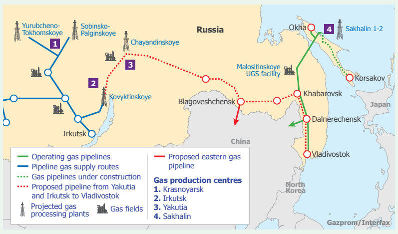
The long-term promise of gas in the US may be punctuated by short-term volatility as coal and gas prices fluctuate over the next two years.

Wildcat Blog

Kangnam style

Myanmar is preparing to offer several prospective offshore blocks, but companies considering moving into the country's crystal blue waters should proceed with caution

Most read



1 China, Russia gas deal set, but clash over price

2 Interconnector outage causes seven-year highs at UK's NBP

3 Gas on the agenda in Cyprus Russia talks

4 Mozambique LNG partners need to be 'nimble' in talks – OIES

5 US producers see production decline in 2013 – Barclays