

# Upstream Internationalization

Challenges and Opportunities

7<sup>th</sup> February 2014



# Agenda

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- ▶ **EY Overview**
- ▶ Upstream Worldwide trends
- ▶ Opportunities in Africa
- ▶ Internationalization strategies

# EY Network Overview

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EY is a leading provider of professional services to global clients



# EY Services Overview

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EY provides Assurance, Advisory, Tax and Transaction services

Assurance	Advisory	Tax	Transaction
<ul style="list-style-type: none"><li>Accounting and Financial Reporting (including IFRS)</li><li>External Audit Services</li><li>Financial Accounting Advisory Services</li><li>Fraud, Investigation and Dispute Services</li></ul>	<ul style="list-style-type: none"><li>Performance Improvement<ul style="list-style-type: none"><li>Strategic direction</li><li>Supply chain and Operations</li></ul></li><li>Finance</li><li>Customer</li><li>People &amp; Organization</li><li>Information technology advisory</li><li>Risk</li><li>IT Risk and Assurance</li></ul>	<ul style="list-style-type: none"><li>Business Tax</li><li>Human Capital</li><li>Indirect Tax</li><li>International Tax</li><li>Transaction Tax</li></ul>	<ul style="list-style-type: none"><li>Transaction Real Estate</li><li>Transaction Support</li><li>Transaction Tax</li><li>Valuation and Business Modelling</li><li>Cross-border Transactions</li><li>Divestments, Carve-outs</li><li>Economic advisory</li><li>M&amp;A</li><li>Private Capital</li><li>Project Finance</li><li>Restructuring</li><li>Transaction Integration</li></ul>

# EY Global Oil & Gas Knowledge Centers

EY has established a global network of more than 9,600 professionals supported by 15 Global Oil & Gas Centers with an extensive experience on the sector, strategically located in areas that allow us to serve best the needs of the oil and gas industry



## Oil & Gas Center roles

- ▶ Anticipating market trends
- ▶ Identifying the services that companies need
- ▶ Provide the right people in the right places at the right time to serve our clients
- ▶ Articulating points of view on relevant key industry developments, trends and issues

# EY offices in Africa



# Agenda

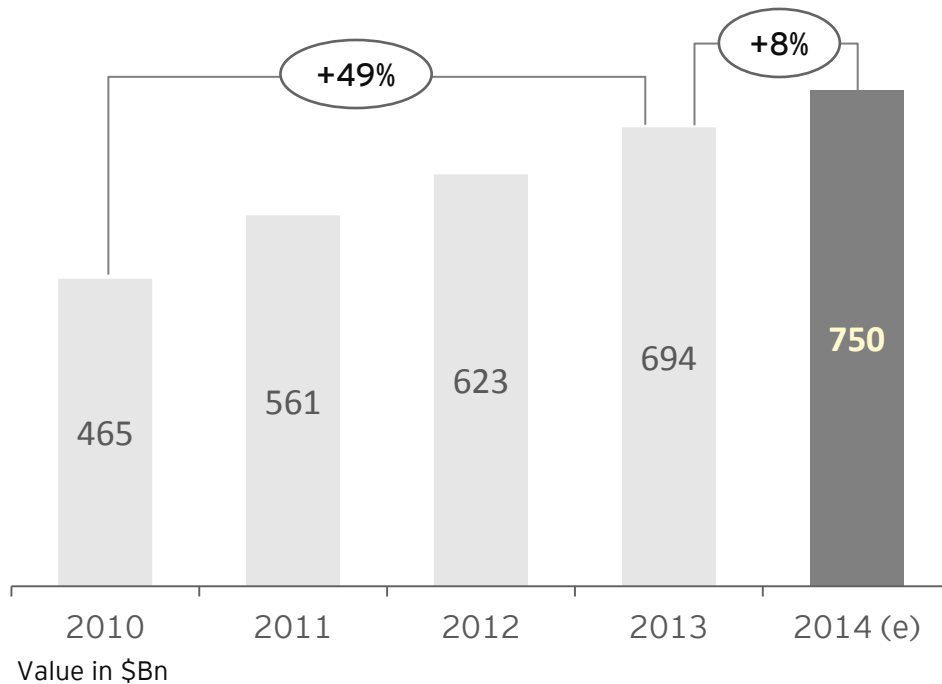
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# Upstream Worldwide trends: Global investments

In 2014 the growth is expected to remain relevant (+8%), even if slightly lower than previous years (+14,3%)

- Upstream 2010-2014 global investments -



- ▶ CAGR 2010 - 2013: +14,3% (Growth 2010 - 2013: +49%)
- ▶ Reasons for the relevant growth expected in 2014 :
  - forecast that Oil price will remain high
  - increasing competition for assets
  - development of unconventional resources
  - replacement of coal with gas - growth in the number of LNG projects
  - new regions to be explored

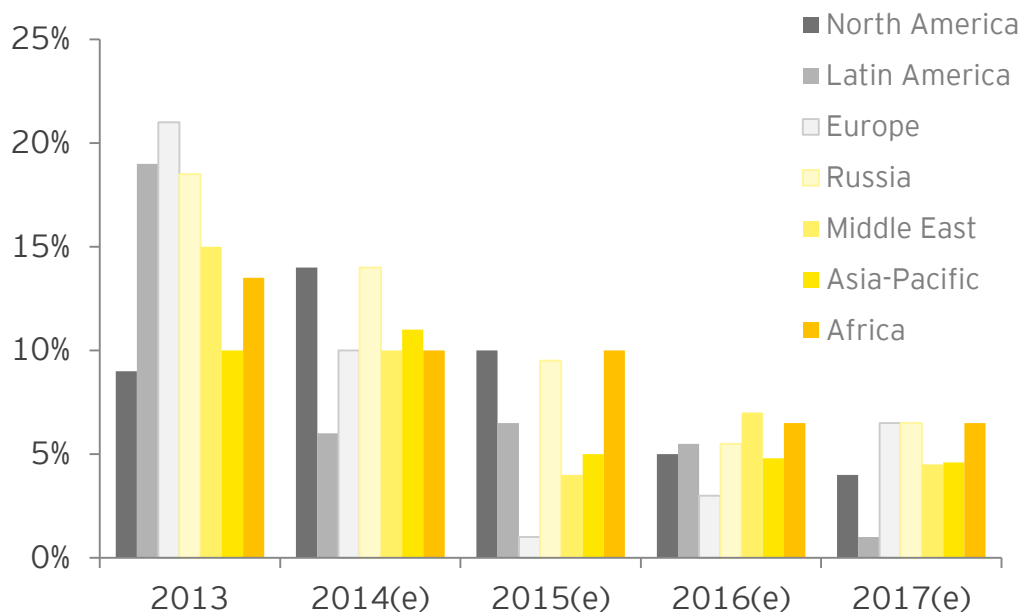
Source: IFP Energies Nouvelle - Investments in exploration-production and refining 2013; EY Oil & Gas knowledge center



# Upstream Worldwide trend: Regional investments annual growth rates

Focusing on 2016 and 2017, investments growth rates will decrease significantly; in Africa the growth is expected to remain relatively high

- Upstream 2013-2017 regional investments annual growth rates -



- ▶ **Middle East growth led by Saudi Arabia**
- ▶ Upstream investment in Europe grown thanks to **North Sea activity and tax incentives**
- ▶ In the **Asia-Pacific region**, considerable investments from national companies in India, China and in South-east Asia
- ▶ **High potential growth in Africa**, slowed due to political and social uncertainties

Source: IHS - The E&P Investment Guide 2013

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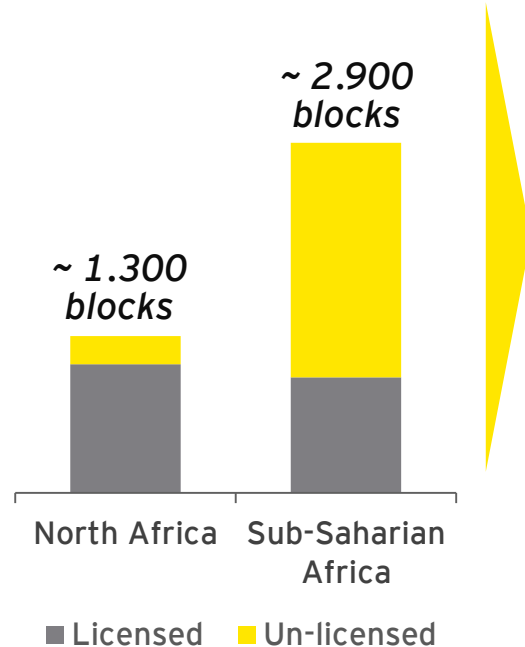
# Focus on Africa: Distribution of licensed and not licensed Oil & Gas blocks

Most of Africa is still unexplored or underexplored: 4.200 Oil & Gas blocks have been identified and more than an half of these are un-licensed, especially in Sub-Saharan area

- North Africa and Sub-Saharan Africa  
Oil & Gas blocks -

North Africa:  
1.300 blocks  
20% of blocks are un-licensed

Sub-Saharan Africa:  
2.900 blocks  
70% of blocks are un-licensed



- ▶ Africa is home to 8,2% world's proved oil reserves and 7,6% of gas ones
- ▶ The Gulf of Guinea and North Africa will remain the main hydrocarbon producing regions
- ▶ East Africa has become the continent's newest energy frontier
- ▶ Due to the gas strikes, the East Africa could become the world's third-largest exporter of natural gas over the long-term

Source: IHS - The E&P Investment Guide 2013

# Focus on Africa: the Sub-Saharan region

As the region is still underexplored with few wells drilled to date, the potential for Upstream companies is very high and it is expected that Sub-Saharan Africa will attract numerous investments in the future

- **Nigeria** dominates the region with a **long-established oil industry** despite the political uncertainty and environmental concerns
- **Equatorial Guinea** and **Ghana** have successfully brought **oil into production** while maintaining political stability ▶
- **Congo** (Brazzaville) is a mature oil province in which **recent field discoveries** have **boosted oil and gas industry** ▶



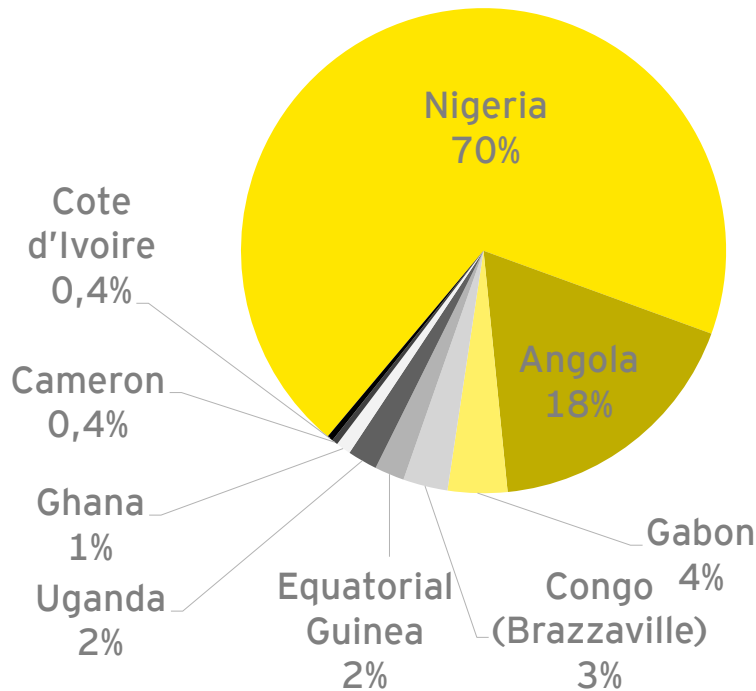
- **Tanzania** exploration activity is taking off with **large international Upstream companies farming-in**
- **Kenya** has been a **hive of activity** over the last few years
- **Angola** is rapidly catching up Nigeria as a **key player in Oil & Gas**
- **Mozambique** will become the **fourth-largest exporter of LNG globally** and **second-largest in Africa** after Nigeria ▶

Source: EY research

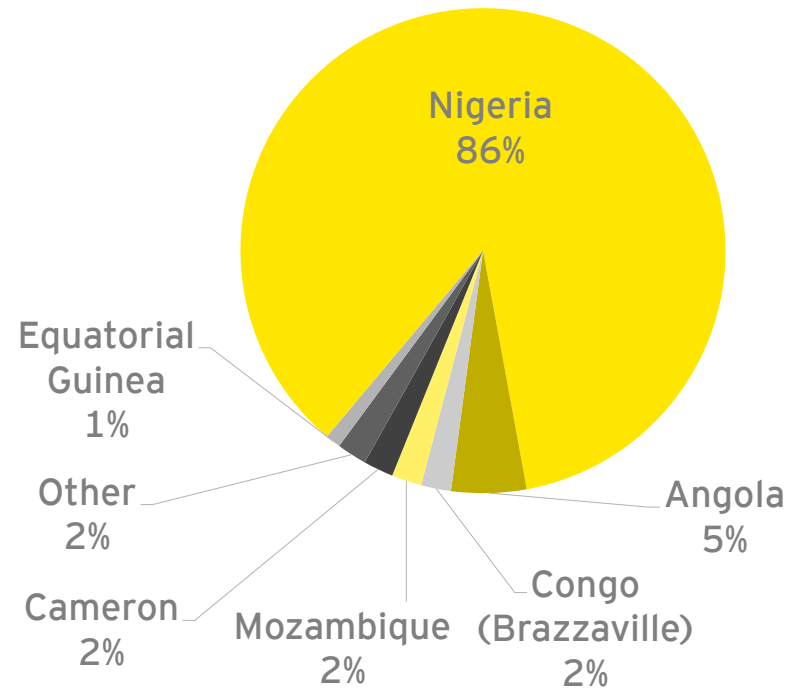
# Focus on Africa: the Sub-Saharan region O&G reserves

Sub-Saharan Africa holds 53.4 billion barrels of proved oil reserves and 208.7Tcf of natural gas resources. This equates to 3.9% of global oil reserves and to approximately 3% of global gas resources

- Sub-Saharan Africa Oil Reserves -  
Onshore & Offshore



- Sub-Saharan Africa Gas Reserves -  
Onshore & Offshore



Source: Scottish Enterprise & Scottish Development International, Spends&Trends 2008-2017, Key Global Oil & Gas Markets Africa - EIA, International Energy Statistics (2012)

# Focus on Africa: Sub-Saharan region risk assessment dashboard

Country	Current overall risk	Risk trend	Political risk	Economic risk	Legislative risk	Taxation risk	Operations risk	Security risk
Angola	■	↑	■	■	■	■	■	■
Benin	■	→	■	■	■	■	■	■
Cameroon	■	→	■	■	■	■	■	■
Congo (Brazzaville)	■	→	■	■	■	■	■	■
Congo (Zaire)	■	↓	■	■	■	■	■	■
Cote d'Ivoire	■	↓	■	■	■	■	■	■
Equatorial Guinea	■	→	■	■	■	■	■	■
Ethiopia	■	↑	■	■	■	■	■	■
Gabon	■	↓	■	■	■	■	■	■
Ghana	■	↓	■	■	■	■	■	■
Kenya	■	↑	■	■	■	■	■	■
Mozambique	■	↓	■	■	■	■	■	■
Namibia	■	↑	■	■	■	■	■	■
Nigeria	■	↓	■	■	■	■	■	■
Rwanda	■	↑	■	■	■	■	■	■
Somalia	■	→	■	■	■	■	■	■
South Africa	■	↑	■	■	■	■	■	■
Tanzania	■	→	■	■	■	■	■	■
Uganda	■	→	■	■	■	■	■	■

Source: EY analysis from IHS Global Insight

■ Low risk   ■ Moderate risk   ■ High risk

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# Upstream services internationalization: key drivers

Upstream-related companies have to consider the above 5 key drivers in the repositioning of their international investments in order to understand the attractiveness of any project

## Concessions & Tax regime

- ▶ Royalty tax system
- ▶ Contractual arrangements
- ▶ Government take

## Operating conditions

- ▶ Upstream value chain integration
- ▶ Upstream technology
- ▶ Infrastructure conditions
- ▶ Costs and outsourcing

## Political framework

- ▶ Macroeconomic fundamentals
- ▶ Political issues
- ▶ Legal framework

## Materiality

- ▶ Resource quality
- ▶ Resource nature

## Geology

- ▶ Number of wells
- ▶ Location of wells

Source: IMD, Ralf Boscheck - Assessing "New" Upstream Business Models



# Upstream services internationalization: main risks areas

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Potential risks have to be addresses also considering the company initiatives portfolio in order to balance the overall investments structure

## Strategic

Increasing market uncertainty and complexity due to new international competitive framework

## Political

Increasing costs and risks due to resources nationalism and lack of transparency in the bureaucratic procedures

## Financial

Increasing risks in achieving the needed financial resources due to the pressure of higher costs of capital

## Operational

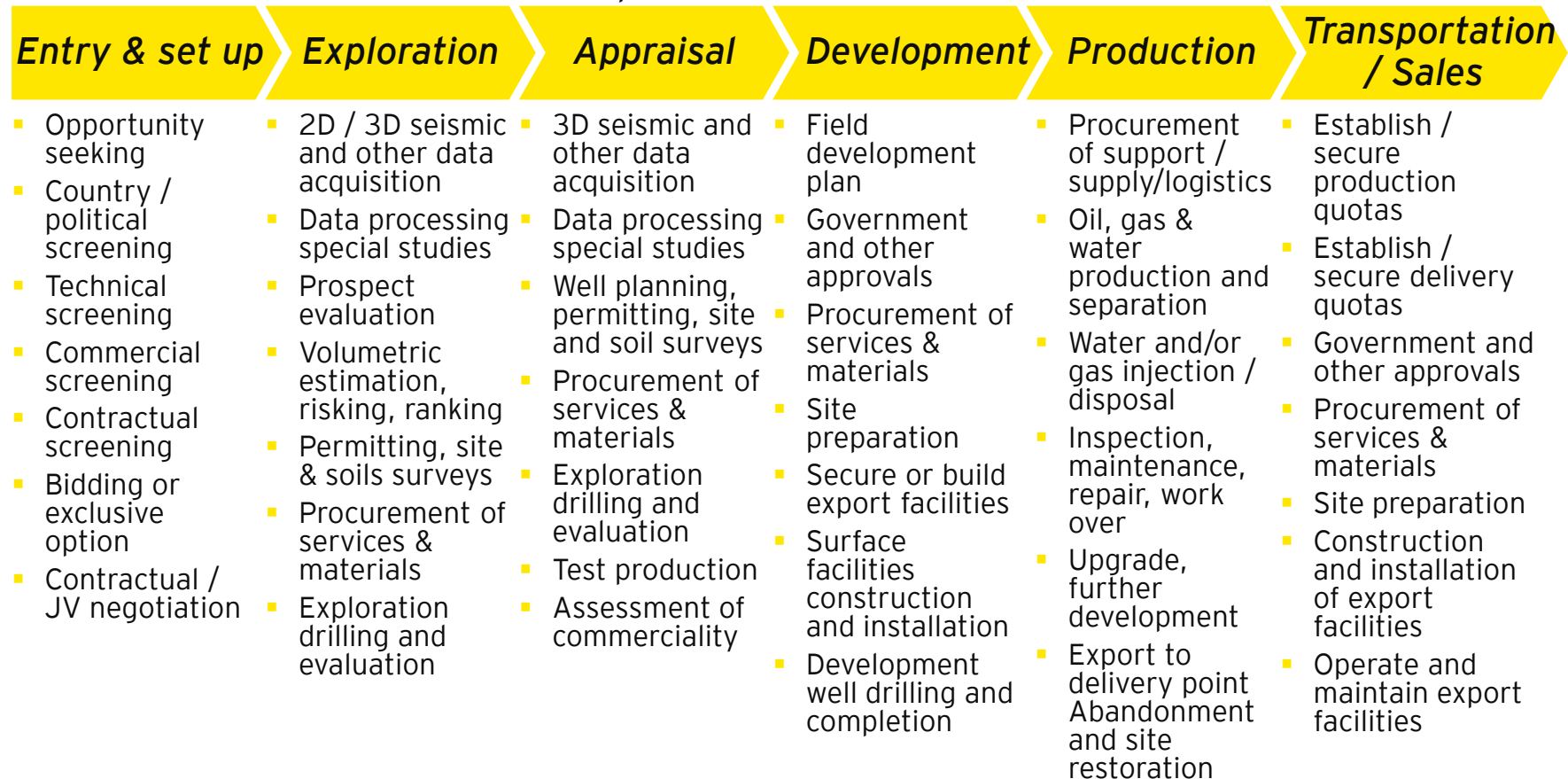
Increasing risk due to the trade-off between operational efficiency and development of new technologies

Source: EY Oil & Gas knowledge center

# Upstream services internationalization: opportunities

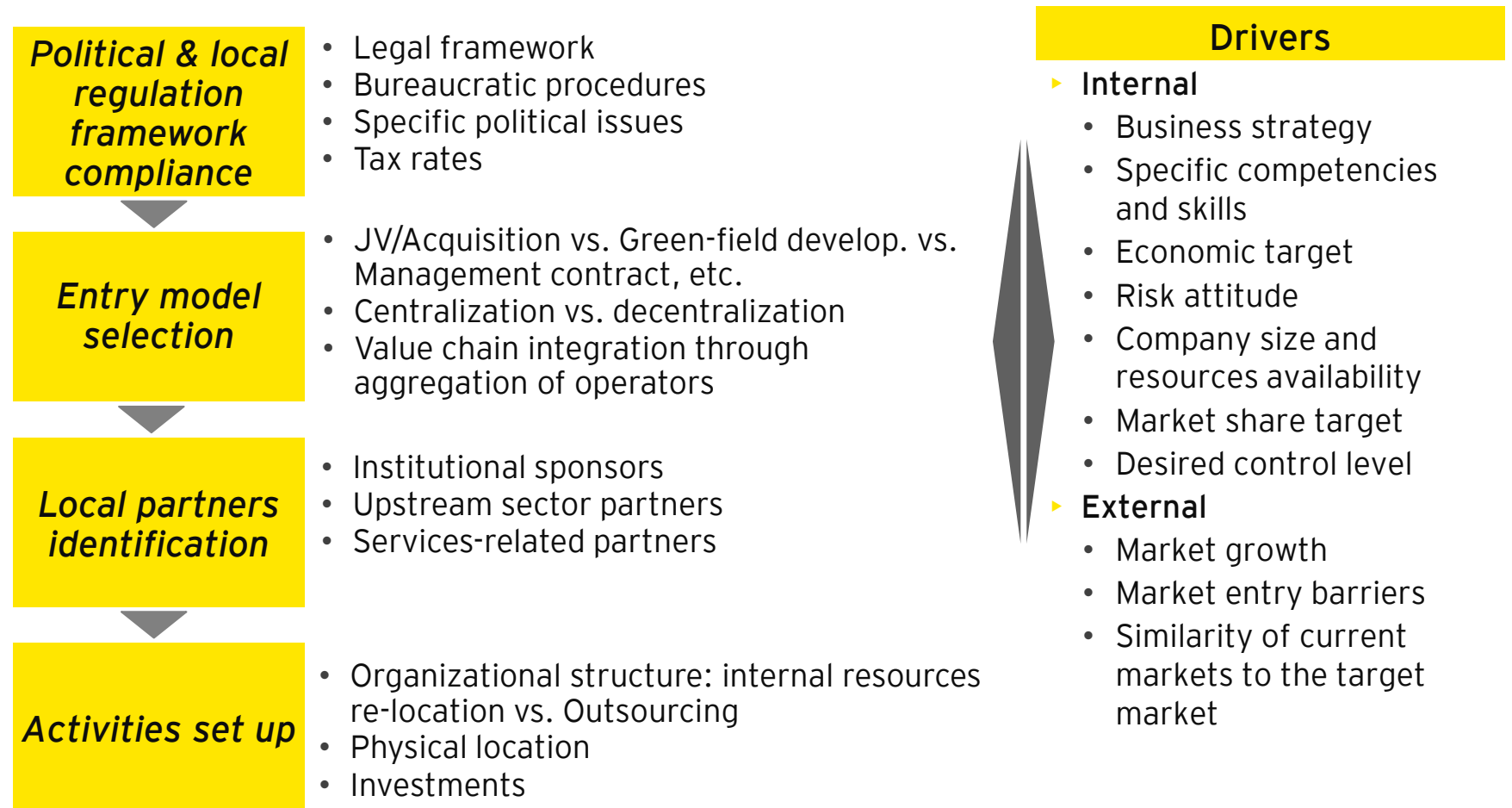
Upstream service providers have to address potential opportunities to exploit along the whole Upstream value chain considering the target country maturity level

- Upstream value chain -



# Upstream services internationalization: steps to set up foreign activities

Upstream service providers should set up following aspects to enable internationalization, considering both internal and external drivers and leveraging on the Upstream value chain



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## Country details

# Focus on Africa: Mozambique



## Mozambique will become in the future a strategic location in the gas Upstream industry

### O&G legal framework

- The proposed **new petroleum law** aims to make the legal framework transparent for investors
- The **5<sup>o</sup> competitive bidding** round is expected in **2014**

### Concessions & Tax regime

- Upstream activities must be carried out through a **concession** awarded by the Council of Ministers under an **open bid**
- **Engineering, procurement and construction (EPC) contracts** are issued for 30 years only under strict government requirements and can be renewed upon request or cancelled in case of failure or bankruptcy
- Tax regime applicable to the oil and gas industry consists of a **combination of CIT and royalty based taxation**

### Operating conditions

- Mozambique takes advantage of **South Africa Gas pipeline**
- The reserves of natural gas could sustain the construction of **10 LNG** plants over the next decade
- Many **Offshore** fields have been discovered in the last three years
- Empresa Nacional de Hidrocarbonetos (ENH), the national oil company, has 10-15% free participation in all blocks



Source: EY research

# Focus on Africa: Congo (Brazzaville)



## Congo (Brazzaville) is among the top five oil producers of Sub-Saharan Africa

### O&G legal framework

- Plans to award around **10 onshore and offshore oil blocks by early 2014** in a new licensing round
- **Plans to reform the Petroleum Code**, but to date no new proposal has been presented

### Concessions & Tax regime

- Upstream operations are governed by **production sharing agreements (PSAs)** which also include tax breaks and a royalty system
- **Tax regime** applicable to the oil and gas industry consists of a combination of **CIT, royalty based taxation, pollution tax and tax on the rental value of professional premises**

### Operating conditions

- Congo holds sizable proved natural gas reserves but only small amounts are commercialized because of the **lack of infrastructure**
- The Congolese civil war left much of the country's **transmission and distribution infrastructure damaged, not restored**
- A vast majority of **oil and natural gas** exploration and production activities are conducted **offshore**
- Congo also may hold large **oil sands deposits**, a potential key-driver for the revitalization of the country's oil industry
- Congo's national hydrocarbon company, **Societe Nationale des Petroles du Congo (SNPC)**, manages Congolese government-owned shares in hydrocarbon operations



Source: EY research

# Focus on Africa: Ghana



## Investment in Ghana's hydrocarbons sector has boomed over the past six years

### O&G legal framework

- The **Petroleum Revenue Act**, passed in 2011, outlines clear mechanisms for collecting and distributing petroleum revenue
- The **Petroleum Commission (PC)** was established in 2012 as the industry regulator
- Petroleum regulations are being drafted with **local content** requirements reaching 90% after 10 years. Furthermore there is a requirement for 10% local participation for subcontractors and 5% for operators

### Concessions & Tax regime

- Exploration and production rights are based on a **30-year production sharing contract** with the contractor bearing all the costs and risks
- **Tax regime** consists of a combination of **CIT**, **royalty based taxation** (from 3 to 10%), **oil entitlement tax** and **surface rental tax**

### Operating conditions

- **Oil and natural gas** exploration and production activities are conducted **offshore**
- Ghana plans to build a **natural gas pipeline** to pipe associated gas at oil fields
- Imports and export come via the **West African Gas Pipeline (WAGP)**, which runs from Nigeria to Ghana
- Ghana's national oil company, Ghana National Petroleum Corporation (GNPC), has a 10% participating interest with the possibility of obtaining another 2.5% in all assets



Source: EY research