NIGERIAN MARGINAL OIL FIELDS – KNOTS IN FUNDING

UBA Capital Partners

Nigerian indigenous firms own more than 50% of the 173 oil and gas concessions in Nigeria so far, but account for less than a tenth of the 2.3 million barrel/day production. This is a paradox of 'idle wealth' that has denied the Nigerian government and people the full benefit of local participation policies.

More precisely, the 32 marginal fields awarded (including the five discretionary awards and NPDC's fields) cumulatively produce around 2.6% of daily oil production and 2.5% of the estimated 4,000 MMscf gas production in the country, due largely to the inability of indigenous firms to fully monetise the assets. Marginal oil fields as defined in Nigeria are oil fields or wells that are nearing the end of their commercial life and whose production rates are lower than 10,000 barrels per day.

While noting the dearth of local technical expertise, given decades of isolated IOCs participation in the upstream oil and gas sub-sector, we think the inability of indigenous marginal field owners/operators to secure adequate funding is a core hindrance to unlocking the underground wealth, especially to achieve 'first oil'. With a March 2015 ultimatum for all marginal field licensees to accomplish optimal operation, we track the salient facts undermining the monetisation of these assets.

While the erstwhile aversion of the Nigerian banking system towards long tenored project finance in the upstream oil and gas sub-sector was a notable barrier to financing, beneath the funding challenge lies the bankability of the assets, given a host of 'soft points' that encumbers the economics of the fields.

To start with, the award process encumbers the asset from the onset, as such fields end in years of litigation. More so, the inaccuracy of the reserve data (beyond tolerance limits), on which the fields were awarded undermines the bankability of the projects. Closely tied to the fiscal process of field awards is the adverse selection of technical and foreign equity partners, leading to inconsistency in field development and production, given fluctuating service level agreements and lopsided cost and earnings sharing negotiations.

While farming has been a traditional source of equity funding for marginal fields, it leaves the indigenous firms at the mercy of foreign equity and technical partners, with less interest in marginal fields, an unbalanced alignment of interest, which slows down the field development. More importantly, the dearth of financial and project advisers on marginal fields have undermined the investment case for accessing funding, especially as the project economics is often fraught with complexities and inconsistencies surrounding taxation, pricing, capital expenditure and funding terms.

Nonetheless, the recently steep trend in local capacity development, engineered by a new generation of indigenous talents with a good match of entrepreneurial and technical skills, should be positive for the increased contribution of marginal fields to overall oil and gas production in Nigeria.

Interestingly, recent success stories and the track record of these experienced locals in translating reserves to cashflow is steadily improving the appetite of local banks for marginal field financing, just as local capacity development of local project finance advisers like UBA Capital and a few peers should provide support for marginal oil and gas project development, going forward. Albeit, in achieving the fiscal local content drive, relevant government agencies need to address the fiscal-related constraints in the awards of oil fields as well as ensure concessional tax regime for marginal field development, given elevated marginal operating cost of the wells.