

Chinese oil giant ventures into Somalia

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CNOOC's willingness to strike an oil deal with the fragile government of Somalia, which has been a failed state for more than a decade, has provided stark evidence of China's willingness to brave terrain that western oil majors deem too treacherous.

The state-owned Chinese oil giant has signed a production-sharing deal with the transitional federal government in the east African country, which ranks as a high-risk frontier even in an industry well accustomed to dangerous environments.

In doing so, CNOOC and its smaller partner, China International Oil and Gas, are gambling on three points. First, that the interim government has the authority to make such deals and will stay in power. Second, that violence stemming from perennial inter-clan conflicts and more recently Islamist extremism will not derail its work. Third and most fundamentally that the country has some oil worth extracting.

Several western oil majors held exploration concessions in Somalia in the 1980s, but fled in 1991 when the overthrow of dictator Siad Barre ushered in 16 years of chaos.

Ali Mohamed Gedi, Somalia's interim prime minister, told the Financial Times last week that ConocoPhillips, Chevron, BP, Royal Dutch Shell and Eni would be invited to return and change their concessions into production-sharing agreements under a new oil law due to be published in the next two months.

But that looks like a distant prospect. BP, Shell and Eni say they still consider the concession deals to be subject to force majeure code for unexpected and disruptive events that prevent contractual obligations from being met. Chevron and ConocoPhillips have declined to comment.

Thomas O'Connor, chairman of Benchmark Oil and Gas and a former World Bank oil engineer who studied Somalia, says: "Many of the companies there in the 1980s have been subsumed into others and the bigger they get the more conservative they become. The super majors will likely talk about it internally, but my guess is the legal counsels will say 'No, let's wait until the dust

settles'."

Chris Brown, a sub-Saharan Africa analyst at Wood Mackenzie, a consultancy, says: "The big issue at the moment is there are three different governments issuing exploration contracts, hence the legitimacy of these licences may be thrown in doubt if there were to be any change in the political landscape."

The government of Somaliland, a northern province that considers itself independent, struck a production-sharing agreement with Ophir Energy in 2003. The government of the semi-autonomous Puntland province has given Range Resources of Australia and Canmex Minerals of Canada joint exploration rights in part of the region.

CNOOC's deal details of which emerged last week covers another part of Puntland and was endorsed by President Abdullahi Yusuf Ahmed, who hails from the province, even though the transitional government's authority there is tenuous. The prime minister himself has questioned the validity of the Chinese agreement because it was signed before the new oil law is in place.

Mr O'Connor says: "Big oil companies are loath to go into dodgy areas where they don't have good contractual relationships. But the Chinese are taking the view: 'Let's just do it and deal with the consequences later.' It's buccaneering."

CNOOC has acquired a reputation for risk-taking a reflection of the fact it is ultimately serving China's strategic need for oil rather than purely commercial objectives.

Insecurity in Somalia was underlined last Thursday when the re-opening of a conference intended to promote reconciliation between the country's clans, warlords and political factions was marred by bomb attacks that killed at least five children near the Mogadishu venue.

Range Resources estimates that Puntland has the potential to yield 5bn-10bn barrels of oil.

The US Energy Information Administration, however, says the country has no proved oil reserves.