

Successful Reform – a Foreign Operators Perspective

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Your Excellencies, Ladies and Gentlemen; Colleagues and friends in the oil and gas industries. It is with great pleasure that I have again returned to Algeria. This occasion is particularly rewarding as I have had an opportunity to meet with so many of you personally and to address you this morning.

In keeping with the aims of this conference and with our Company's knowledge and role in Algeria, I would like to share with you our views on the subject of ways in which we, as a foreign operator, can play an active, and we hope valuable, role in any process of reform. Reform, which I know we all wish will lead to more investment in the energy sector and consequently to greater export potential and prosperity for all concerned.

However, before talking about reform, let me briefly tell you a little bit about our Company and our current activities.

Burlington Resources is a global super independent, meaning that we do not participate in downstream refining and marketing activities. The majority of our production is derived from North America, where we control one of the largest positions of natural gas, an environmentally friendly fuel that has come of age. In fact, we have seen a four-fold increase in the wellhead price of natural gas in North America during the last twelve months. We are the fourth largest holder of and the fifth largest producer of North American natural gas reserves. The larger holders include household names like Exxon Mobil and BP Amoco.

Due to the maturity of hydrocarbon basins that exist in North America, Burlington Resources finds it appropriate to expose itself to the large reserve potential found in less mature producing provinces around the world. Although only a little more than 10% of our current production comes from outside North America, our other global operations provide us the growth engine for the future. It is that potential for growth, which has attracted us to Algeria.

In Algeria, Burlington Resources is the operator of the Block 405 in the Berkine Basin and has been active here since 1993. We have acquired comprehensive 3D seismic coverage over our entire block – making this shoot part of the largest contiguous onshore 3D survey in the world - and we have drilled a total of 24 wells.

With this very extensive work program, we have made numerous discoveries, including a portion of the giant Ourhoud field, the MLE gas field and two field complexes; MLN in the north and MLSE in the south.

In this part of the Berkine Basin, most of the oil and gas fields have been found in relatively thin reservoirs and in subtle traps. As a result, we have needed to make extensive use of modern seismic and have had to drill a large number of wells to both locate and delineate these discoveries. While our exploratory success rate is exceptionally high, the individual field sizes are small, averaging less than 100 mmbbls oil equivalent. Furthermore, we have encountered

various forms of hydrocarbons, including black oil, gas-condensate and dry gas, further complicating our development plans.

The Ourhoud field is now being developed by the Sonatrach and its partners and is expected to commence production in late 2002. The MLN main field received Ministerial approval last year and front-end engineering design work is now nearing completion. The MLN construction work and development drilling will be carried out through 2001 and 2002, with a first oil production set to occur at the end of 2002.

Keeping to that first production date is one of our primary goals – for reasons that I will explain in more detail later. However, with some \$30 million spent on seismic and over \$200 million spent on so far on wells, I think the economic significance of passing time will be very apparent to you.

As a long-standing and active participant in the development of Algerian oil and gas reserves, what then is our appropriate role in the reform process?

Firstly what do we mean by reform? Well, if I understand it correctly the reforms that are envisioned here in Algeria include the simplification of the regulatory process and a significant increase in transparency. These major steps are aimed at increasing Algeria's global competitive position. Algeria must compete in the world arena for both capital investment, and for energy export market share.

Companies such as my own which are participants in many countries around the world are in effect the customers in this situation. International or global companies are free to select where they invest based on their assessment of the risk and the potential reward. In the 1990's, the globalization of the industry has become near complete and we are no longer constrained by geography. We have many choices of where to invest, and our investment will go to those places that are viewed as globally competitive. This is especially true of exploration in new areas.

The presence of these "market forces" where the international energy industry supplies resources – capital, human and technological – is a major influencing factor in shaping the industry for the 21st century. If opportunities in a particular country are not competitive, then investment will go elsewhere. Perhaps that is what this chart is telling us was occurring in the late 1990's in Algeria.

So how then can we, the global foreign operators, aid Algeria in making its reforms effective? It seems to us in Burlington that the most obvious way is to be open and honest, as we would always chose to be with our friends, partners and colleagues. We can then be very clear and direct in working together and thereby help to speed up the impact of these "market forces". Burlington has made this offer to assist on several occasions and the offer remains open today. These competitive forces are I believe inevitable. Therefore, the quicker they are acted upon, the quicker incremental investment will flow in to the country's energy sector.

As an example of this openness, Burlington, in collaboration with the other foreign operator members of the Algerian Petroleum Club developed an eight-point letter, which was sent to Mr. Bouhafs at his request during the spring of 2000. We were very pleased to receive that request as it indicated a true desire to work in partnership.

After a great deal of careful consideration we realized that our proposals were close to those already under consideration. That letter set out the main areas where the foreign operators saw the need for improvements that would either directly or indirectly increase foreign investment.

Almost all the points of that letter, which I will highlight shortly, dealt with processes and not with the fiscal terms.

The industry is well used to the concept that high quality opportunities, such as those in the Berkine Basin, attract a higher than average fiscal burden – that is part of the demand-supply balance in the upstream industry. What is very much less acceptable to the international investor is the erosion of the value of these opportunities through slow, bureaucratic or cumbersome processes that delay monetization. This is an obvious source of inefficiency that impairs investment competitiveness and was the principal target of the proposals being made by us last spring.

To briefly summarize the main points made in that letter:

- The traditional role of Sonatrach as licensor, regulator and partner was seen as one of the principal sources of inefficiency. We are all now well aware that the separation of these duties is one of the main planks of legislation proposed by the new administration and will hopefully be in force this year. We applaud the Minister's efforts in this regard and look forward to assisting in any way we can to bring about these changes.
- The time to negotiate contracts and the frequency of re-negotiation has always troubled the foreign operators in Algeria. Again we see some moves underway to implement a streamlined model contract, and to simplify and speed up the finalization of contracts. This effort needs to be strenuously pursued through to practical application.
- Harmonizing the decision-making processes of the various parties has the potential to increase efficiency greatly. Increased transparency in the agencies being developed under the new law will help this process as will the focus of Sonatrach as a competitive oil and gas company.
- A particularly critical phase in the value creation associated with our industry is the decision of whether to, and how to, develop the resources we discover. This is a time when the decision-making and transparency need to be emphasized. Failure to do so is a certain way to erode value. Value that is lost to inefficiency at this stage is lost to all parties; the Algerian State being the largest stakeholder has the most to lose.
- As transparency increases, there is seen to be huge potential for valuable input from all sectors of the industry. Changes can then be more effectively and quickly implemented. Consultation has the major advantage of increasing investment confidence.
- Overly prescriptive labor practices, additional training and improved performance management processes are areas that must be addressed in order to allow the industry as a whole to rise to the challenges of international competitiveness. This is one of the most fundamental challenges that Sonatrach will need to confront as it assumes its new role as an internationally competitive oil and gas company.
- Any improvements in the administrative practices, which reduce delays and the associated costs, should be aggressively pursued. The delegation of sufficient authority to the individuals charged with managing assets is an important aspect of this issue.
- Finally, the infrastructure needed to support the industry needs to be developed to agreed standards and in a way that facilitates access to all parties in a transparent fashion.

We at Burlington, along with our partner Talisman Energy, have invested over \$300 million in Algeria and have discovered more than 300 million barrels oil equivalent of producible reserves. Anywhere else where we operate this would be the grounds for great celebration – however, here

in Algeria we remain concerned as to whether and when we will be able to achieve a competitive return for our shareholders.

Our circumstance is perhaps different from some others, but does however represent a situation that may increasingly arise in the future, as the Berkine Basin matures.

The Burlington discoveries are individually small and complex. This complexity has required us to use extensive seismic and numerous wells; which means we have incurred high exploration costs. The variability of the fluids and the multiple, relatively thin, reservoirs have caused the development costs to also be high.

Let us look then a little more closely at the economics of our discoveries.

After recovering the high finding and development costs, paying export tariffs and, the proposed charges for water and electricity that are being imposed on us, there is very little profit remaining below the 49% revenue share limit from which a competitive return can be generated.

The ways by which we can improve the return are not new, but nevertheless bear listing and comparing with the various issues that the international industry identified in 2000 as key to future investment confidence.

These issues apply equally to oil as well as gas discoveries, although the processes associated with gas reserves are even more problematic. However with the full collaboration of the Ministry and Sonatrach we are looking forward to significant progress on our gas discoveries in the near future.

The avoidance of delays is a key factor and perhaps the most critical. Delays erode the value of the money that has been invested and in the case of Block 405 those costs have been substantial. In addition, the capital we have tied up here represents an opportunity cost, because that capital could have been released to be used elsewhere.

The success of small field development requires the processes – physical and organizational – be as streamlined as possible. Over specifying either physical plant requirements or overly complex approval processes will add to costs and time erode value.

The use of new technology and the importation of new ideas is often a key to success. Regulatory procedures need to be adapted to this situation. I am not talking about “cutting corners”, rather the elimination of waste.

And, finally we must eliminate any unnecessary costs.

I hope you have noted that we have not proposed that the fiscal terms have to be relaxed – that would certainly be nice and we would naturally encourage its consideration – all we have suggested is that the Algerian petroleum sector undergo the necessary reforms to render it more competitive and efficient in the international investment arena.

Additional value is then created, and can continue to be shared by all the parties involved. To conclude then.

We believe that reform is vital to improving the health of your petroleum industry. We further believe that there is a very critical role for us and other foreign operators to play in this process. We all need to work together to bring these changes about and Burlington Resources is prepared to carry its fair share of that burden. We applaud the efforts of the Algerian Government and His Excellency the Minister of Energy and Mines in particular in his efforts to bring about reform.

Thank you for your attention.