Maximising local benefit

INTERVIEW WITH AIDAN HEAVEY
CHIEF EXECUTIVE, TULLOW OIL PLC

AIDAN HEAVEY is a founding Director and shareholder of Tullow Oil plc. He played a key role in the development of the company from its formation in 1985, to its current international status as a leading independent oil and gas exploration and production group. As a chartered accountant, he previously held roles in the airline and engineering sectors in Ireland. Mr Heavey is a director of Traidlinks, an Irish based charity established to develop and promote enterprise and diminish poverty in the developing world, particularly Africa.

What is the history of Tullow Oil's involvement in Namibia's Kudu gas field?

We started looking at this project about four years ago when we were in negotiation with Chevron, who had a stake in the field at that time. During that period Energy Africa, which was the major shareholder in Kudu, also went up for sale. When we bought Energy Africa and all its African interests we also acquired 90 per cent of the Kudu field, but this was really a very small part of the company's portfolio in terms of value. The major value lay in its producing fields and projects in other African countries such as Equatorial Guinea and Gabon in which they played a role as a 'silent partner'. Tullow Oil, on the other hand, is a company that has a great deal of experience in operating projects in Africa. In fact, the first project we ever did back in 1987 was a gas to power project in Senegal, West Africa. Therefore we were able bring a lot of experience of operations and related gas utilisation deals to Kudu.

The first thing we did was a complete review of what had been done in the past. We put together a team of experts in order to review all the field data and initiated new studies in relation to potential onshore developments. We then started discussions with NamPower, the Namibian national power utility, in relation to their power demands and began negotiations on a gas purchase agreement.

What is the current climate in terms of bringing such Gas to Power projects to fruition?

Originally, when Kudu was first discovered, it was thought to be a giant gas field and then, following the initial hype, expectations diminished. Also, at the time, it was viewed as 'stranded' gas. Gas prices were extremely low internationally and there was plentiful cheap power generation available in the region from coal-fired power stations in South Africa, which was effectively subsidised.

However, the world has changed over the last few years with energy prices going through the roof, from \$20 up to \$65-70 per barrel for crude oil, with gas prices moving accordingly. Also there is now an increasing demand for gas and energy – even in South Africa which has had problems with shortage of power.

Kudu has consequently changed its status. It is now no longer viewed as a 'stranded' gas field, but a field that could have huge commercial value for Namibia. Our only partner in the Gas to Power project, until recently, is NAMCOR, the National Petroleum Corporation of Namibia, which is owned by the government, so we are looking at all the various alternatives to make sure that the Namibians can get the maximum benefit from their resource. We therefore revisited all the seismic and technical work done on the field to date and decided that we should drill some new exploratory appraisal wells to see if we can prove up additional gas in the licence. This would then create the potential for other projects in addition to the power generation project, such as the export of gas.

The current volume of gas, which is around 1.2tcf, can be brought onshore to supply an 800 megawatt power station. That would meet all Namibia's power needs and would even allow Namibia to export to other parts of Africa.

If the exploratory appraisal programme comes up with proven additional gas, then there would be the potential for additional power generation or other gas development projects, depending on how we could maximise the overall benefit to the country. The ultimate size of the field could be 8-9 tcf.

Could a gas-fired plant in Namibia export electricity to South Africa at a viable cost?

If we are building an 800 megawatt power station, we would have to look at Eskom as one of the customers for it. If we can prove a bigger resource and increase the size of the Kudu field then that has a knock-on effect because the production investment costs will be spread over a larger amount of gas, which will reduce the gas prices accordingly. From the point of view of the government, the tax earned from the increased volume sales, when netted back against the gas prices, would make the power project even more cost effective.

What is the timetable for that additional exploratory work?

We started the exploratory appraisal drilling programme in May and by October we should know whether or not the Kudu field is bigger than was previously thought.

Apart from NAMCOR, who are the other partners in this project?

NAMCOR have 10 per cent interest in Kudu and we have recently brought in the Japanese group Itochu, for a 20 per cent stake, subject to partner and government approval. We had been approached by a lot of companies who wanted to get involved but in the end we went with a company that could bring added value to the consortium, and who had international LNG and pipeline expertise. We therefore have a very good partner in Itochu.

To what extent is the regulatory and economic environment, both locally and regionally, a major variable in the potential of this project?

Generally, it is not easy to develop a field like Kudu in Africa because financing is a major problem due to the value of local currencies etc. I believe we are very fortunate in our timing because the investment climate at the moment is extremely good. People are looking very positively towards this project and the impact on the region in terms of economic development will be huge. It is not just about having your own source of power generation; governments also get large tax revenues from it.

To what extent can the exploitation of petroleum resources make a difference to the socio-economic development of Africa in general?

Tullow Oil is currently involved in fourteen countries in Africa. We have been involved in Africa from day one. I started the business in 1986 in Senegal, so Africa is in our blood in relation to these projects. We are very aware that the historic reputation of the oil industry in Africa has not been good to say the least. Since the company started we have had a policy of investing in local communities long before we start producing our oil and gas, and we have followed that approach in the different countries all over Africa. We invest very heavily upfront in community projects – if they don't have schools or hospitals we make sure they get them, as well as roads and other basic infrastructure. We also make sure that local companies and local people supply services to the industry, which directly helps to uplift the economic lives of people in the country. We make sure that our operations are run by locals and put training programmes in place to make sure that they get the best long-term education and experience in the sector. The future is to ensure that local skills are running our projects and not a lot of expats.

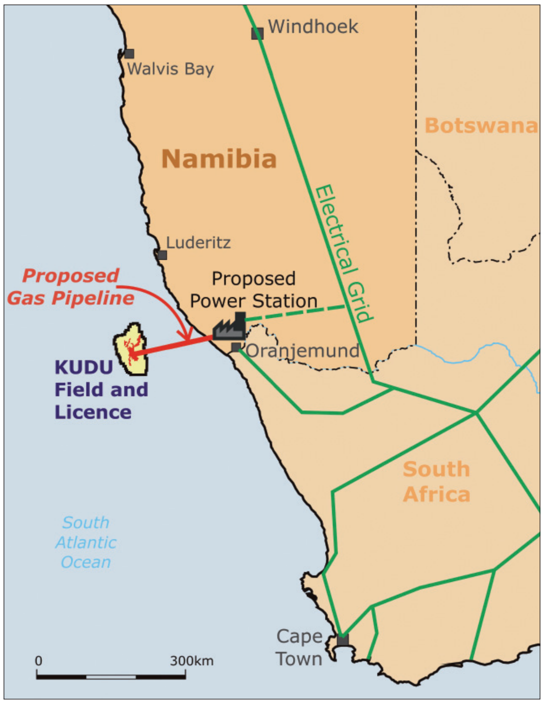
How do you view the political risk of operating in Africa?

People asked me years ago 'what the political risks were of being involved in Africa' and I said the biggest political risk country in which we had a bad time was the UK, where the Chancellor could change his tax regime twice in a year. We have now been in Africa for twenty-one years and it has been a pleasure; nobody has changed the terms of our deals and the governments we have worked with have been extremely supportive.

We take a very long-term approach to our strategy, which is Africa based, although we do have operations in other parts of the world. When we go into countries, we stay for the long term and we develop a major business there. It is a slightly different approach from that of the smaller exploration companies who go in and drill wells and then sell out, or the major companies who are just after a specific product, which is mainly oil, to sell to their refineries. They don't often get involved in power projects, for example, because the return may be too long-term for them. We actually like those sort of projects – that's what we started off doing. We can do the same job as a major oil company, yet we have the flexibility of a small one.

Another advantage when starting off early in a development, is that you can do it right from day one. That is hugely beneficial in the long run because the project can immediately start working from a social point of view. I think Namibia is in a great position, as is Uganda, for example, to learn from the lessons of the past. Our projects in Namibia and Uganda will be a major component of our overall investment of £350 million in 2007.

Tullow Oil has been growing very rapidly over the last five or six years. Today our market capitalisation is US$5 billion. We currently produce 80,000 barrels of oil a day, which makes us the biggest independent European producer right now. That is a dramatic level of growth from a base of 2,500 barrels per day in 2000, and it has mainly been in Africa. Now we have the financial clout to do the deals that we always dreamt of doing – and the Kudu gas field project has been one of those. F



The impact of the Kudu gas field project on the region in terms of economic development will be huge

A map showing the Kudu gas field, the proposed gas pipeline and power station