China and CNPC are consolidating further their positions in Iraq petroleum sector

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Introduction

Four years after the first bid round took place some IOCs are consolidating their positions while others are descending after good start and some were even unable to make an entry. CNPC stand among the first group while ExxonMobil exemplify the second group and many known IOCs, such as Chevron, Repsol and Conoco Phillips fall among the third group.

In a previous paper I addressed how Russia has entrenched and solidified its role in the Iraqi petroleum sector.[1] This paper is mainly about CNPC path of consolidating its presence in this sector.

Recently, two high ranking Iraqis and CNPC confirmed ExxonMobil offer and on Thursday, 28 Nov 2013, the deal was signed involving stakes to CNPC (China) and Pertamina (Indonesia) in the super giant West Qurna 1 (WQ1) oilfield.[2] This deal, with undisclosed sum, is now the fourth success in a row for CNPC which could surely solidify its profile in Iraq, and deepen China's position in the Iraqi economy and the energy sector, specifically petroleum. The Chines companies accepted low remuneration to serve company and national strategic objectives and could have practiced transfer pricing, through sub-contracting, to factor-in for lower remuneration fees and to augment their financial gains.

The partial framing-out of ExxonMobil from WQ1 has many implications. CNPC' consolidation has, from strategic and operational perspectives, its pros and cons for both Iraq and CNPC alike; further weaken American IOCs' role and finally, provide an opening for Pertamina in post 2003 petroleum sector.

CNPC's fourth success in a row

CNPC is the only foreign oil company that is involved in three oilfields and just involved in a fourth one[3], making it the leading company and thus consolidating Chinas position in Iraq' upstream petroleum**.**

Alahdab, in Wasit province, was its first success story, when in a proven act of pragmatism CNPC accepted in November 2008 conversion of the production sharing contract signed in 1997 into long term service contract-LTSC.

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[1] See my article, ***Russia Consolidates Its Position In Iraq Upstream Petroleum.*** MEES 55:35, 27 August 2012. http://www.mees.com/en/articles/5795-rusia-consolidates-its-position-in-iraq-upstream-petroleum Also posted on IBN: http://www.iraq-businessnews.com/2012/08/25/russia-consolidates-its-position-in-iraq-upstream-petroleum/

[2] See http://www.iraqoilreport.com/business/companies/update-exxon-splits-west-qurna-1-stake-cnpc-pertamina-11569/?utm_source

[3] Though Shell has more horizontal involvement through WQ1, Majnoon and BGC contracts.

Two significant interrelated outcomes of that move: CNPC was the first IOC making entry into petroleum upstream post 2003, and thus opened the door for other IOCs. Second, Alahdab contract, despite its many disadvantages for Iraq in comparison with the LTSC that followed it[4], had actually shaped the versions of the LTSCs that were used for the four bid rounds.

The field, discovered in 1979 and estimated to have about 1.055 billion barrel proven reserves covers 200 km^2. The work on the field started in March 2009 and by June 2011 its output reached 60 kbd, half a year earlier than planned. $1.5 billion, out of $3 billion budgeted for the entire oilfield, was spent up to July 2011. The second phase, with 120 kbd capacity, was completed by end 2011, and again three years ahead of schedule, allowing CNPC picking up the first cargo of 650k barrels of oil on 29 December 2011.
By mid- November 2012 production reached 140 kbd from 170 operational wells. The third phase would upon full completion bring production plateau to 200 kbd, instead of the contracted plateau of 115 kbd, as requested by CNPC.

Oil goes through pipelines from the field to Tuba oil storage in Basra, then to export terminals. The contract specifies providing dry gas to the nearby Al-Zubaidiya power plant and delivery of all LPG to the LPG bottling plant in Kut town (the capital of Wasit province). It is worth mentioning that Al-Zubaidiya power station was awarded to China's Shanghai Heavy Industries in 2008. The first two units with 330MW each started operation and another two units scheduled for completion bringing total production to 1320MW by end of 2013. Two further units will be added in 2014, bringing total cost of the entire power plant to $2.4 billion. When fully completed, the plant fuels by 15 kbd oil, later runs on dry gas from Alahdab field, supplemented by gas from southern oilfields.

The second CNPC success is **Rumaila** oilfield. Due to CNPC direct efforts BP/CNPC consortium was able to win the one and only deal during the first bid round held on 29/30 June 2009, after reducing their remuneration fee from $3.99/b to $2/b.[5] Moreover, CNPC managed to increase its participation interest in the consortium from 33.33% during bidding time to 49.33% soon afterwards. Some $15 billion investment is expected in the field, which has 17.8 billion barrels of proven reserves, over 20-year duration of the original contract. The success of CNPC even at that early stage had prompted the US embassy in Baghdad, through official communication, to accuse some of the advisors in the Prime Minister Office of favouring the Chines against the American oil companies.[6]

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[4] For evaluating Alahdab contract see my commentary: Al-Ahdab Oil Contract Has Many Flaws (Commentary posted on IBN, July 2011) **http://www.iraq-businessnews.com/2011/07/26/alahdab-oilfield-began-production-but-its-contract-still/**

[5] See my article, **Lessons To Be Learned From Iraq's First Bidding Round.** MEES v52n33, 17 August 2009.

[6] For further information on this official memo see Tactical Newswires, 17 December 2009, at Tactical Report Website, http://www.tacticalreport.com

BP and CNPC spent about $1.5 billion for work in 2010 that raised output and thus received their first payments in May 2011 at 2 million barrel oil each after reaching the contracted 10% incremental threshold above the 1.066 mbd initial production rate-IPR agreed in December 2009. By end June 2011 about $1 billion was paid to them through a total of five tanker loadings each worth roughly $200 million. Therefore what was spent in 2010 was recovered in 2011 through oil deliveries.

The field was producing 1.35mbd in July, will average 1.45mbd for 2013, and aims for 1.55mbd in 2014. Annual budgets for 2011 to 2013 was 2.5, 2.2 and 2.85 (in $billion) respectively. The contracted plateau is 2.850mbd sustainable for 7 years, but BP/CNPC proposed three lower plateaus and longer periods- a high scenario of 2.4 mbd, a medium scenario of 2.2 mbd, and a low scenario of 2 mbd. Any of those changes could affect field development plans for 2014 thus the matter has to be decided before 2013 ends.

By the end of 2012 BP and CNPC had received a total of $4.5 billion for their investments in Rumaila oil field[7], and this has particular significance for both BP and CNPC in recycling their revenues to finance next year work program and thus positively impacting the economics of the project and ensuring a very rewarding internal rate of return-IRR.

Halfaya is CNPC's third success. CNPC is the operator with (37.5%) participation interest along with two junior partners, Total and Petronas (18.75%) each. The field has 4.94 billion barrel proven reserve (at 34.1 recovery factor of an estimated 16 billion barrels of oil in place) and large volume of gas was contracted to reach a plateau of 535kbd in 2017 sustainable for 13 years.
The first phase of developing Halfaya was completed by mid-June 2012 with 100kbd crude and 90mn cfd of gas, again, as was the case in Alahdab, 15 months ahead of contracted time limit, with planed increase to 200kbd by end of 2013 at investment of $920 million, according to Iraqi official sources. Investment payback began ahead of schedule. On mid-December 2012 the first cargo with 2 million barrels of oil was lifted and a second cargo was lifted by late January 2013. This oilfield is first to become operational and begin investment recovery amongst the green oilfield offered under the second bid round.
The second phase of the project was launched and on 14 April 2013 CNPC announced it had started construction of a 100kbd facility with 60 drilled wells, due to come on stream in the second quarter of 2014. A new 272km crude pipeline to Fao will be critical for phase 2 scheduled completion. The final phase would push the capacity to 600kbd, higher than the contracted 535kbd, by end-2016, CNPC said.

Under the contract IOCs are responsible for processing associated gas against similar remuneration fees per barrel of oil equivalent-boe. Hence CNPC began, in May 2012, work on a $36 million project to process associated gas and pipeline it to Al-Kahla power plant, completed in 2010 providing 180 megawatts. The project anticipates 50 mscfd of gas, of

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[7] As reported by IBN, see http://www.iraq-businessnews.com/2013/09/22/bp-cnpc-get-4-5bn-rumaila-payment/ accessed 26 Sept 2013

which 80% to Al-Kahla, and the remaining for the power plant built by CNPC for Halfaya purposes. The pipeline completion would allow CNPC receiving remuneration fee for oil and for the processed associated gas.

In addition to the above mentioned development of Halfaya oilfields, CNPC has also finished a small local airport comprising one runway of 1700 meter and 30 meter width suitable for small aircrafts of 50 passengers. The airport will be used to commute workers and light supplies between Halfaya and Basra international airport. Halfaya contract does not cater for this airport, and thus it is assumed that this project is part of CNPC voluntary contribution – a form of corporate social responsibility.

Finally, CNPC is making its fourth success by acquiring 25% stake in **WQ1** and this acquisition would surely consolidate CNPC position and makes it the leading IOC in the upstream petroleum. And with the other Chines companies, China becomes the top ranking country in Iraq's petroleum sector.

Profile of the Chines IOCs in the Iraqi upstream petroleum

Two Chines oil companies are currently involved in the upstream petroleum and the following table summarizes the profile of their involvement.

	Number of Fileds	TPPT (mbd)	WARF ($/b)	PR (Bbl)	TIP (mbd)	PPC (mbd)	NRF ($m/d)
CNPC	4	6,41	2,052	32,391	5,1	2,111	2,43
CNOOC	3	0,45	2,3	2,5	0,35	0,27	0,314
Total	7	6,86	2,068	34,891	5,45	2,381	2,744

Source: Author's compilation from related LTSCs and MoO data.

CNPC and China National Offshore Oil Corp -CNOOC are involved in five LTSCs pertaining to developing seven oilfields. CNPC has participating interest with other IOCs in Rumaila, Halfaya and WQ1 (pending formal approval) and Alahdab (on its own), while CNOOC is the operator of the three Missan oilfields of Buzurgan, Abu-Gharab and Faqqe (with junior partners Total and Petronas).

Total proven reserve (**PR**) of these oilfields is close to 35 billion barrels (Bbl), constituting a quarter of Iraq's official proven reserves. Oilfields with CNPC involvement have 32.4 Bbl of proven reserves, while those with CNOOC involvement have 2.5 Bbl of proven reserves. For two Chines companies to have such huge involvement in so much proven preserves is significant strategic advantage, even when these involvement are in partnership with other IOCs.

Total production at contracted plateau targets (**TPPT**) from these oilfields is 6.86mbd, most of which comes from CNPC-involved oilfields. Again, the Chines IOCs have critical involvement in Iraq's total production whether plateau production for Rumaila and WQ1 remain unchanged or reduced, pending negotiations.

Total incremental production (**TIP**) for these oilfields over baseline production would be 5.45 mbd, constituting ca. 79.5% of their combined contracted plateau production targets. This percentage would increase gradually due to the assumed natural decline rate in the base line production for the oilfield contracted under the first bid round.

Except Alahdab the Chines companies are partners with other IOCs in the development of these oilfields. Thus, based on their participation interests the Chines contributions in total production plateau (**PPC**) is 2.381 mbd, constituting 34.7% of combined plateau production from these oilfields.

Remuneration fees paid for the development of these oilfields range between $1.4/b (for Halfaya) and $6/b (for Alahdab). However, the weighted average of remuneration fee (**WARF**) (weighted by production level) is calculated at $2.07/b.

Based on their contracted remuneration fee total of what the Chines IOCs earn, at plateau production, in net remuneration fees (**NRF**), after deducting the State Partner share and the corporate income tax would amount to approximately one billion dollars annually. These remuneration fees could increase further if the allowances for processing associated gas from Alahdab, Halfaya and Missan fields are included.
The above estimation of fees was based on R-factor value of less than one, and this is why it is a maximum (without counting the allowances for processing associated gas). These maximums could be reduced further when R-factor value exceeds one as stipulated in each contract of the above mentioned fields. For Alahdab the R-factor reduces realized remuneration fee to 50%; for Rumaila and for WQ1 to 30% and for Halfaya and Missan fields to 20% of their contracted remuneration fee.[8]

I would argue that remuneration fee was not the prime target for CNPC and CNOOC, rather it was the venue to access and gain strong hold in the Iraqi petroleum sector for the strategic objective of securing access to vast, low cost reserves and with geographical proximity. Without this strategic objective it would be extremely difficult to explain or even contemplate how could CNOOC agreed, after nearly eight months from the date of the first bid round, to reduce its remuneration fee from $21.4/b to $2.3/b! Not only this but when Sinochem, the joint Chines bidder in June with 20% participation interest, opted out CNOOC found another junior partner, the Turkish TAPO, easily and quickly.

[8] For discussing the factors affecting the remuneration fees see my articles, **Benchmarking The Remuneration Fees For Iraqi Oil Fields.**' MEES v52n44, November 2009, and **Remuneration Fees Are Measured In Cents, Not Dollars!**. MEES v53 nr 11, 15 March 2010.

I would argue further that remuneration fees are not the only source of earning for the Chines companies. In fact "cost inflating" through sub-contracting to other Chines service providers and companies is a major source of significant financial gains. The most obvious and comparable cost item is well drilling activities, as briefly discussed below.
In 2010 BP/CNPC awarded contracts for drilling 49 wells to reach Zubair reservoir (at depth 3200 meters) with a total cost of $500 million. Out of these wells 21 were awarded to Iraqi Drilling Company- IDC (jointly with Schlumberger) and 21 to the Chines company- Daqing and 7 wells to Weatherford. Reliable sources say contracted cost per well are as follows: IDC: $10 million; Weatherford: $11 million and Daqing: $12 million.
Also earlier in March 2010, the Turkish Co. (TPIC) won a $318m deal to drill 45 new wells at Rumaila field, at an average cost of $7 million per well.
A formal itemized drilling cost estimation-IDCE for four wells in Rumaila (RU-364, RU-367, RU-376 and RU-377) among the above contracted 94 wells gave an average cost of $4.7 million per well, while credible sources asserts that actual drilling cost by TPIC was $3 million per well! Finally, the IDC had a contract with ENI to drill 12 wells to Zubair reservoir (in Zubair oilfield) at a turn-key cost of $5 million per well. The following table calculates the excess of Daqing's drilling cost compared to (i.e., over) those drilled by others.

	Daqing' excess drilling cost ($ million per well)
TPIC-Contract	5
TPIC-Actual	9
IDCE	7.3
IDC	7

Source: Author's compilation

The above narrative indicates that, assuming other things been equal, the Chines Co, Daqing is the most expensive for drilling operations, where it's cost is higher than others by a range of $5 million to $9 million per well.
This in my view could indicate to transfer pricing practice raising suspicion why the Ministry of Oil permits such questionable disparities in drilling cost within one filed and mostly to the same reservoir; and whether the Inspector General of the Ministry of Oil had investigated this matter, which this author raised in an elaborated public communication dated 1 April 2010.

The same pattern of excessive drilling cost could have existed for Missan fields. As recent as September 2013 CNOOC awarded $347.85 million worth for drilling 39 production wells. Weatherford was awarded two drilling contracts worth $94.98 million and $82.39 million respectively. China's Bohai Drilling Engineering Company-BDEC won a $96.66 million contract and China Oilfield Services Limited- COSL, a specialized oil services unit of CNOOC, was awarded a $73.82 million drilling deal. The average drilling cost per well is $8.92 million, though it was not clear yet how many wells each company would drill.[9] Hence,

[9] In a recent article, dated 27 October 2013, by the Senior Director of Accounting at Missan Oil Company-MoC he mentions $11 million drilling cost per well compared with $3 million

it is not possible to make meaningful comparative assessment on whether Chines drilling rates in Missan fields follow similar pattern to that in Rumaila. Also since IDC is the State Partner in the service contract for these three oilfields, it was not possible to get a share in the drilling contracts probably out of “conflict of interest” principle, yet COSL did!

On the pipeline side the Chines companies play crucial role in the development of the oilfields operated by CNPC and CNOOC. A 42-inch-diameter pipeline was built by China Petroleum Pipeline Company **(**CPPC**)** in cooperation with South Oil Company (SOC) and local government in Missan and Basra. It starts from meeting point of the two lines from Buzurgan and Halfaya down to Fao. Also it includes installing five cathode stations, eight electrical valves, pump station, systems of and central control unit in Halfaya field, in addition to sub-stations in Buzurgan and Fao. For the time-being no further information is available to make any comparative or standardised cost assessment.

In early October 2013 Missan Oil Co., (MOC is one of the Ministry of Oil’s State companies) announced that CNOOC has introduces new world technology using enforced plastic pipeline (RTP) to transport crude oil and connecting wells at Abu Gharab oilfield.

The success of this first experiment in Iraq could have serious cost-saving implications, and thus the Ministry of Oil should commission or undertake a technical and economic feasibility study as soon as possible and draw practical recommendations for using RTP since the pipeline requirements are very substantial under any production scenario.

Despite its apparent successes CNPC had faced with resentments from local communities in both Alahdab and Halfaya oilfield. These local concerns are related to variety of issues such as land compensation, employing local people, increased pollution, road accidents among others. Also, domestic politics has its role as the conflict between local governing councils and central government erupts now and then.
Recently, Alahdab site was raided by gunmen assaulting both Iraqi and Chinese employees and stealing and money and computers.
For Halfaya, CNPC has begun hiring and training local villagers and farmers to provide security and increase local employment. Moreover, The Halfaya project has an immediate goal of training and hiring 250 locals for jobs in security, mechanics and electrical engineering, according to MOC media manager and vacancy announcement posted on the Ministry website in October 2013.

Other Possible Opportunities
CNPC might have further opportunities in the petroleum sector. ENI indicates willingness to have CNPC onboard with other partners in Zubair oilfield and Lukoil still hoping to have CNPC as partner in WQ2 oilfield.
A member in Kirkuk provincial governing council has reportedly said they held talks with CNPC regarding Kirkuk oilfield. Thus the recently signed Letter of Intent- LoI between the

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for similar wells in the neighboring countries. See the article in Arabic on http://www.kitabat.com/ar/page/27/10/2013/18443

Ministry of Oil and BP, worth at least $100 million, provides 18 months of technical assistance and consulting to arrest the decline at the field and provide options for reversing that trend, could more likely involve CNPC in the future substantive work replicating the Rumaila consortium, which MEES considers as, “one of the more successful joint ventures”.[10]

In addition to CNPC and CNOOC other Chines companies might get significant chunk in the refining sub-sector. A big Chines delegation, including CNPC, attended Nassiriya Integrated Project (comprising field development and construction of advanced refinery with 300kbd capacity) second Amman workshop of mid-September 2013, and the recently concluded MoU with Satarem for Missan advanced refinery (of 150 kbd capacity) could involve Chines participation.

The State-owned China Petrochemical Corporation (known as Sinopec) held talks with Lukoil about jointly developing the West Qurna 2 oil field, but Lukoil’s chief executive Vagit Alekperov said: *“*Unfortunately, the Iraqi government didn’t confirm joint work with Sinopec.”[11]
It is worth mentioning that Sinopec was part of the ENI consortium qualified for Zubair oilfield in the first bid round of June 2009. But when the company purchased in 2009, and before concluding the Zubair deal, Switzerland’s Addax Petroleum, which had an oil contract with the KRG, and thus was disqualified and then blacklisted. Since then, Sinopec was prevented from and still unable to participate in projects in central and southern Iraq.
To have access to Iraq’s upstream petroleum Sinopec could learn something from the Indian Reliance Industries-IRI.
Reliance was re-qualified in 2013 by the Ministry of Oil to bid for the Nassiriya Integrated Project –NIP scheduled for mid-December after IRI ended, in July 2012, its contracts with KRG signed in 6 November 2007.[12] It is worth mentioning in this regard that Reliance Exploration & Production DMCC's had 80% interest and operatorship of the PSCs covering Rovi and Sarta blocks, while OMV Rovi GmbH and OMV Sarta GmbH, hold the remaining 20%. The blocks are located north of Erbil and cover a combined area of approximately 490 square miles (1,124 square kilometers). Chevron purchased Reliance’s assets in July 2012 for $200 million, prompting Baghdad to blacklist Chevron and thus prevent it from any future projects. If Sinopec wants to have a foothold in WQ2 or any other upstream petroleum project it should follow IRI pathway.

Further and Concluding Remarks
It is obvious that Chinese companies’ strategy was to use low remuneration fee as their venue for accessing and consolidating their position in the Iraqi upstream petroleum. In this respect they are the most successful among all IOCs in applying this classical strategy. The availability of vast and diversified sources of logistical services, professional manpower, supplies and subcontractors helped them also to be the most successful executing companies.

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[10] See MEES (Vol. 56, No. 45, 8 Nov 2013)
[11] See http://www.iraq-businessnews.com/2013/10/15/sinopec-is-dealt-a-setback-in-iraq/
[12] http://www.iraqoilreport.com/business/companies/five-more-firms-get-nassiriya-bid-approval-11174/

This, through possible transfer pricing practices, could help in compensating for low remuneration fees. Even if transfer pricing was not practiced, the effect of the contracted upstream petroleum projects have significant value and impacts for China from macroeconomics (multiplier effect at home) and strategic (access to energy sources) perspectives.

The Iraqi authorities had earlier set the end of December 2012 as deadline for ExxonMobil to sell its share in the field due to its deals with KRG, but obviously, that did not occur. When CNPC and Pertamina deal for WQ1 is accepted it is of vital importance for the Ministry of Oil to expedite the process and finalize the needed contractual arrangements as soon as possible in order to prepare the final development plan for WQ1.
Moreover, the ministry should consider imposing **capital-gain tax** on ExxonMobil resulting from selling part of its shares. The ministry in collaboration with the Taxes Public Authority should prepare the premises and estimation of the capital-gain tax before the ministry gives its authorization of the share transfer pursuant to the "Assignment" article of WQ1 contract.

Not only CNPC is consolidating further its contribution to the upstream petroleum development projects, but both BP and Shell are doing the same. This is evident by important recent development such as BP's recent LoI regarding Kirkuk oil field and Shell horizontal involvement in WQ1 and Majnoon oilfields (upstream petroleum), in Basra Gas Co.,-BGC (gas industry) and the recent concluded Head of Agreement-HoA for $11billion petrochemical complex in Basra (downstream).[13]
On the other hand ExxonMobil is on the downtrend, by its own making, and could eventually exit WQ1 completely probably not in a very distant time, as senior Iraqis have hinted! When that takes place there will be only one American company, Occidental Petroleum-Oxy, remain involved in the upstream petroleum as junior partner within ENI consortium in Zubair oilfield. Further information indicates that Oxy is contemplating trimming its presence in the Middle East to have more stakes in the fracking activities in the US. While big American IOCs have limited and declining presence in Iraq upstream petroleum the American service companies, such as Schlumberger, Baker Hughes, Weatherford are thriving very well indeed.

By taking a 10% stake in WQ1, Pertamina makes its first entry in Iraq's upstream petroleum post 2003. More than ten years ago this company concluded a production-sharing "Exploration and Development Contract" in 2002 for the "old" exploration blocks 3 in south western desert. But the contract has been "frozen" and cannot be reactivated until it is converted into service contracts, as senior Iraqi oil official had reportedly said. The ministry of oil could take this opportunity and be more proactive and take the initiative by converting this old contract into a contract similar to that used for the fourth bid round.

China as a country and CNPC as IOC possess strategic significance for Iraq generally and for oil marketing in particular. A recent study by Wood Mackenzie suggests China will become the largest crude importer in the world over the next seven years, surpassing United States by

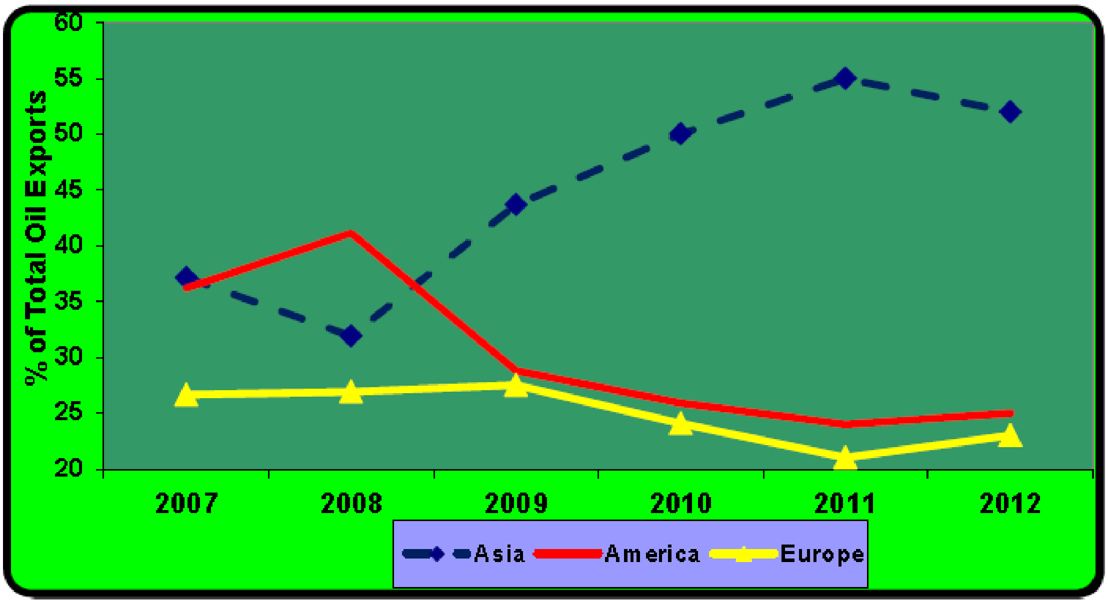
[13] Though the works on Majnoon and BGC still under the previously declared thresholds.

2017, and OPEC suppliers, who traditionally focused on the U.S, will be compelled to shift their focus towards China. According to The Financial Post, analysts believe 66% of China's oil imports will be from OPEC by 2020, compared to 52% in 2005.[14]

This significant change in the global energy outlook is partly due to the real implications of Fracking revolution- use the techniques of hydraulic fracturing and horizontal drilling to tap oil and natural gas trapped in shale rock- in the US and partly due to demographic and growth prospects in East Asia region, especially in China.

According to the US Energy Information Administration (EIA) Iraq was the sixth largest net exporter of petroleum liquids in the world in 2012, with the majority of its oil exports went to refineries in Asia, to Europe and to the United States; China's share from total Iraqi oil export was 13%.[15] The following chart, which uses aggregated Iraqi official data, demonstrates increasing orientation towards East Asian markets since 2008.

Iraqi Oil Export to Regional Market Destinations (2007-2012)



Source: Author's compilation based on data from MoO and SOMO

Recent information indicates that China has already made a request for 0.9-1 mbd for 2014 and the MoO is considering whether it can meet all the additional requests. In this respect it's worth mentioning that China's State-owned Sinochem Corp is planning to use Iraqi crude oil for 40 percent of the capacity of its new 240 kbd Quanzhou refinery.[16] This comes in addition

[14] http://www.pennenergy.com/articles/pennenergy/2013/08/chinese-oil-imports-to-grow-significantly-by-2020.html?cmpid=EnlDailyPetroAugust212013

[15] See http://www.eia.gov/countries/cab.cfm?fips=IZ

[16] http://www.iraq-businessnews.com/2013/11/04/iraq-beats-kuwait-to-chinese-refinery-deal/

to the 200 kbd of Basra Light crude Sinochem usually buys, though most of which goes to Chinese refineries owned by Sinopec.

Senior Iraqi officials assert frequently that the incremental increase in oil production is aimed mostly at Asia – China, Japan, India and other Asian countries. This is also evident by the scale of export capacity expansion in northern Arabian Gulf; and also the recently adopted Integrated National Energy Strategy-INES calls for similar eastwardly orientations based on its calculated netbacks.[17]

The payment in-crude for CNPC and CNOOC entitlements- investment, remuneration fees and other dues- would secure oil deliveries to the companies for more than two decades to come. Also other Chines companies are widely involved in other sectors of the Iraqi economy in addition to these upstream petroleum projects. Dues to these other companies could also be paid in oil deliveries in case of cash shortage for whatever reasons or due to tight market conditions.

The production of crudes with different API and sulfur content spectrum, and the construction of new refineries with technology capable of handling wider range of crude qualities could facilitate marketing Iraqi oil in China.

The bilateral Iraqi-Chines economic cooperation is usually reviewed and articulated through regular government-to-government meetings and agreements that remain operational and useful even though the contracts, such as upstream petroleum projects and others, are usually premised on commercial criteria.

But on the other hand there could be significant risk for Iraq to let two Chines companies, i.e. CNPC and CNOOC, involve in the development of seven oilfields, which are very significant from production and reserves perspectives.
One could correctly argue that the two Chines companies are actually not alone in these major projects (except Alahdab for CNPC) as the participation interests indicate. Therefore such risk would be shouldered by other IOCs: BP, Shell, Petronas, ExxonMobil, Total and TAPO. That's true; nevertheless CNPC could have significant leverage which Iraqi authorities should consider seriously, especially if Total and ExxonMobil are eventually forced to sell all their shares due to their involvement with KRG.

Undoubtedly, consolidating Iraqi oil position in Asian market and China in particular has significant long-term strategic advantages for Iraq, but as INES asserts, reliance on a single market or a single rout carries risks.

Note: earlier and much shorter version of this paper was published by MEES, Vol. 56. No. 48, 29 November 2013.

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[17] PMAC and World Bank, Integrated National Energy Strategy 2013-2030. Final Report prepared by Booz & Co., June 2013.

Norway, 3 December 2013