

BI-WEEKLY OIL REPORT

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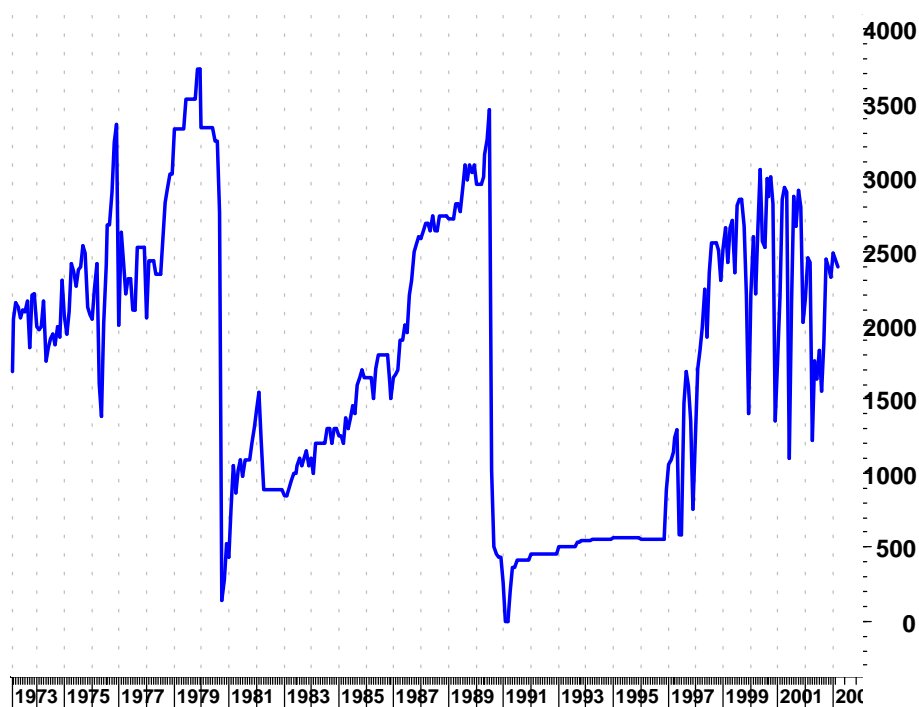
With war talk intensifying during the past weeks, heated debates pro and against military operations and many countries ready to defy international organizations or put at risk long held relationships, one cannot avoid wondering why is the international community spending so much effort over Iraq. Is the threat that Saddam Hussein's regime poses to the international community so grave, or is there a great prize to be gained. Since most of the political arguments and military plans have been over-analyzed lately, we will instead focus on the Iraqi oil industry and its strategic position in today's scheme of things.

Figure 1. Iraq's Saddam Hussein



One cannot measure Iraq's significance to the world's oil markets simply by looking at the country's current production. Iraqi oil infrastructure has been hampered by consecutive wars that started in 1980 with the offensive against Iran and continued with the Gulf War in 1991. As a result very few infrastructure projects have taken place during the last 20 years, while a lot of sites, destroyed during the wars, have never been repaired. Iraqi oil production had reached a peak of 3.5 million barrels per day, before the Gulf war and has never fully recovered since. During the last six years under the Oil-for-Food program it has managed to partially recover, but has remained extremely volatile.

Figure 2. Iraqi oil production (thousand barrels per day)



Source: International Energy Agency

Analysts believe that under current conditions, sustainable production is not higher than 2.8 to 2.9 million barrels per day.

This picture, however, is not representative of the country's potential. Iraqi proven oil reserves stand today at 112 billion barrels and are second behind S. Arabia's 260 billion. Even this number, however, underestimates Iraqi production potential. Due to the continuous wars, lack of spare parts and equipment and the reluctance of oil companies to invest amid extreme uncertainty, only 10% of the country has been explored. The Western Desert field is estimated to hold more than 100 billion barrels of reserves and rough estimates put total Iraqi reserves between 250 to 300 billion barrels. As the Guardian put it "...this means Iraq has a quarter of the world's oil". To get a better idea of the slow development of its oilfields, only 2000 wells have been drilled in Iraq so far, compared with the 1 million in Texas!

Figure 3. Proven petroleum reserves

Country	Proven Reserves (billion barrels)
S. Arabia	259
Iraq	112
UAE	96
Kuwait	94
Iran	93
Venezuela	65
Mexico	48.8
Russia	48.6
Libya	30

Source: Energy Information Agency

Iraq does not only possess extremely rich oil reserves, it also has very low production costs. Estimates put exploration and production costs close to \$1-\$3 per barrel. Only Saudi Arabia has comparable cost structure. Russia, the world's 2nd largest oil producer, has an average per barrel cost of \$9 to \$11.

Iraq's main oil production, today, comes from two fields Rumaila and Kirkuk. Because of the lack of sophisticated equipment and spare parts, as well as the damage of many facilities, authorities have used short-term solutions for pumping as much oil as possible with the existing infrastructure. As a result the situation is deteriorating continuously. A report by the Council of Foreign Relations and the Baker Institute compiled on Dec. 2002, notes among other things the following:

- a.** Iraqi oil infrastructure is in bad shape and production is reduced by 100,000 bpd every year.
- b.** Oil production increase will require massive repairs and reconstruction costing billions of dollars and taking months if not years.
- c.** Costs of repairing existing oil export installations will reach \$5 billion, while restoring output to pre-1990 levels will require another \$5 billion and \$ 3 billion per year as operating costs.
- d.** Possible conflicts between companies over contracts could delay developments even further.

Iraqi government trying to address the issues has proceeded in signing several contracts with foreign oil companies for both old and new oilfields. The agreements amount to an estimated \$40 billion and their full implementation could add 4.7 million bpd of production. Following is a list of all the oilfields and the companies involved.

Figure 4. Iraqi oilfields' development

Oil Field	Proven (Probable) Reserves in Barrels	Company	Cost
Manjoon	20 billion	TotalFina Elf (France)	\$3-4 bn
		Lukoil (cancelled) (Russia)	\$3.7 bn
West Qurna	15 billion	Tatneft (Russia)	
		Rosneft (Russia)	
		Zarubezhneft (Russia)	\$380 m
		Basneft (Russia)	\$190 m
East Baghdad	+11 billion		
Kirkuk	+10 billion	Tatneft (Russia)	
		Zarubezhneft (Russia)	
Rumalla	+10 billion	Zarubezhneft (Russia)	
		CNPC (China)	
		Mashinoimport (Russia)	\$160 m
Bin Umar	+ 6 billion	Zarubezhneft (Russia)	
		TotalFinaElf (France)	\$3.4 bn
Halfaya	5 billion	BHP (UK)	
		Agip (Italy)	\$2 bn
Bal Hassan	2 billion	Tatneft (Russia)	
		Zarubezhneft (Russia)	
Buzurgan	2 billion		
Khabbaz	2 billion		
Nasirya	2 billion	Eni (Italy)	
		Repsol (Spain)	\$1.9 bn
Khormala	2 billion		\$250 m
Ratawi	2 billion	Shell	
		Petronas (Malaysia)	1.3 bn
		CanOxy (Canada)	
Abu Ghirab	1.5 billion		
Tuba	1 billion	ONGC (India)	
		Sonatrach (Algeria)	\$500 m
		Petramina (Indonesia)	
Gharaf	1 billion	Japex (Japan)	
		TPAO (Turkey)	\$500 m
Suba-Luhais	0.5 billion	Slavneft (Russia)	
		Mashinoimport (Russia)	\$300 m

Sources: EIA, Platts Global Energy, Washington Post

It is easy to observe that Russian and French companies have obtained the lion's share of the projects at hand, while US and UK companies are excluded, due to both the UN sanctions as well as the hostile relations with the Saddam regime. Some 300 Russian companies are doing business in Iraq and by late 2002 they had acquired the rights to sell almost 40% of the country's oil. France is Iraq's largest trading partner and TotalFinaElf plays a dominant role in the country's oil sector.

Summarizing the situation in Iraq one could note the following. This is probably one of the most, if not the most, oil-rich country in the world, with minimum production costs, pressing needs for infrastructure projects worth billions of dollars. It is also a country where US companies cannot participate, under the current regime, in any of the existing or future projects.

A regime change would trigger a total reallocation of Iraqi oil assets possibly in favor of the US companies and against French and Russian interests. The above conditions create an explosive cocktail that more than justifies the extreme anxiety among the rest of the world, and the willingness of many countries to sacrifice existing relationships, anger their allies etc. in order to position themselves strategically and influence future developments in their favor.

In this worldwide tag-of-war, it seems that neither the fear of recession for the western world nor the possible destabilization of the Middle East could turn the tide. The stakes seem to be so high that Saddam, the Iraqi people, and even public opinion worldwide seem trivial. Iraq possesses a hidden treasure that everybody wants to put its hands on.

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