How Angola can win back scarce oil investment dollars

The investment budgets of oil companies are at a low and countries such as Angola must radically reform their tax, and other, incentives if they want a share

As the oil price was on its downward spiral from an all-time high of $147 per barrel circa mid-2008 to bottom out at $26 in early 2016 many development and production projects became unprofitable. Suddenly, the principal criteria driving the investment decisions of oil majors, independents and even national oil companies were no longer the size of potential reserves or the prospects of a particular area but rather more objective considerations around low production costs and operational efficiency.

Several countries hitherto considered safe bets for the oil industry fell out of favour with investors because of their high-cost environment. Angola, long seen as a costly country in which to operate, is among the producers most affected by the oil price tumble.

If Angola wants to retain its status as a leading African oil producer in the long run it must decisively move towards offering a more cost-efficient environment for present and future operators.

While some cost levers (labour and housing, for example) can only be applied gradually as the economy cools down after its oil price peak period, certain actions could be taken in short order that would markedly improve Angola's attractiveness for oil investors.

Rethinking the tax regime

An overhaul of the petroleum tax system would go a long way towards achieving the goal above.

It is widely accepted that the 'fiscal terms' offered to oil companies in Angola – broadly understood to encompass the taxes proper and the contractual economic terms – are not good enough to attract either large capital developments or the exploration of more marginal resources. When oil companies run their business models for new developments at the current $50 per barrel range their numbers often do not add up on the basis of the existing fiscal framework.

The Angolan government is acutely aware of this, which is why last year it enacted Presidential Decree 2/16, of 13 June 2016, which creates a set of tax incentives for the development of marginal fields in the form of exemptions, rate reductions and capital uplifts, among other things.

However, the decree seems to have fallen somewhat short of the industry's expectations and seems unlikely, by itself, to kick-start the development of economically challenging resources that require deeper incentives to reward the risk.

But without the development of these resources Angola will struggle to maintain, let alone increase, its production level of 1,700,000 barrels per day.

In light of this the oil industry would no doubt welcome a comprehensive tax reform initiative, especially of backbone statue Decree 13/04 of 24 December 2004 (the 'Petroleum Activities Taxation Law').

It appears the ideal is already brewing in government circles as public statements about improving Angola's fiscal attractiveness have become more frequent as of late. However, no formal move has yet been made in this respect.

Other measures

It is encouraging to see that the government has taken some steps to revamp other oil industry laws outside tax. Just last month a working group was appointed by the Ministry of Petroleum (Order 72/17 of 22 February 2017) and charged with revising the Petroleum Law (Law 10/04 of 12 November 2004). This is long overdue as the Petroleum Law is widely seen as being out of sync with the needs of the oil industry in the context of low prices.

It is anticipated that the law will be modified, among other things, to allow for greater operational and contractual flexibility to enable oil companies to run more cost-effective and leaner operations.

The days when Angola, and other oil producing countries, could afford to impose almost any terms on international investors are long gone.

The investment budgets of oil companies are at a low point and every dollar available must be allocated and spent efficiently and wisely. Countries have to scramble for those scarce dollars and those that are less expensive will have an edge. This must be an absolute priority for Angola today, and in the coming years.

By Rui Amendoeira, head partner of oil & gas, VdA Vieira de Almeida

rla@vda.pt

www.vda.pt/en