Op-Ed

Building Partnerships for the Post Easy Oil Era

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Partnerships have always been integral to the oil industry. But just like the industry as a whole, their shape and structure have profoundly changed over time.

Throughout the first half of the 20th century, technology, expertise and financial capabilities were firmly in the hands of international oil companies (IOCs), making them the dominating players in their partnerships with the governments of hydrocarbon-rich states, including in the Gulf, that were keen on developing their resources.

With resource nationalization in the 1970s and 80s, the balance of power began to shift away from IOCs to the national oil companies (NOCs) that controlled the hydrocarbons on behalf of their governments. But IOCs' technical expertise and financial strength still remained integral to resource extraction.

Over the past 20 years, partnerships in the industry have undergone yet another period of transformation. NOCs today control more than 90% of the world's oil and gas reserves, compared with less than 10% in the 1970s, which has enabled them to build up their own technical and financial capabilities – and strengthen their position vis-à-vis IOCs. Today, NOCs may opt to partner with IOCs on an equal footing or challenge them as competitors in projects anywhere in the world.

As recently as 2010, the concept of NOC-IOC partnerships was alive and kicking, focusing on cooperation in the development of harder-to-reach reservoirs as the world entered the era of post-easy oil. However, with the onset of the unconventionals revolution in North America, new methods of boosting oil and gas output emerged, prompting companies into new types of tie-ups with partners that offer different skill sets and technologies. As a result, inter-industry partnerships have become more complex.

With the oil industry's evolution continuing amid ongoing technological advancements that bring ever-more-remote hydrocarbons within their reach, partnerships are likely to become even more diverse going forward. Today, the industry may still talk about NOC-IOC cooperation, but a wave of new partnerships is under way between NOCs and independents, NOCs and service companies, as well as national international oil companies (NIOCs), NOCs and IOCs. The list of combinations doesn't end here.

The trend is driven by technology as well as economics. The new frontier in oil and gas production involves two very different sets of projects: mammoth ones, which are commonly located offshore and often complex, expensive and technologically more demanding to develop; and small to medium size ones, with very different fundamentals that are mostly located onshore.

On large offshore projects it is unusual even for large oil companies to singlehandedly stem the cost, manage the risks, and provide the technology required to produce the hydrocarbons. On these projects, a pooling of resources—whether among IOCs or between NOCs and IOCs—will be the most likely scenario, depending on the rules set by the host government. Before the unconventionals revolution, this is how partnerships were mainly pursued and thought of.

For smaller-scale onshore projects, the size of companies getting involved tends to be smaller too. Still, the costs involved in developing these schemes are often too high in comparison to the financial muscle of these firms. New forms of partnerships, including between independents and NOCs, are emerging in this space too.

The relevance of partnerships is also changing due to the need to manage country risk in various parts of the world as production becomes more transnational. This is especially the case for NIOCs, who will have to learn to partner with both the private and the public sector to manage risks better. This is an area where IOCs have developed an advantage, but NOCs are beginning to catch up.

The evolving industry landscape isn't just changing the shape and structure of partnerships between companies, but also between producers and consumers, in particular in the area of natural gas. Many consumers want to open a new era of partnerships with producers – one that relies on a new gas pricing mechanism and a more diversified set of suppliers. These consumers want to replace the current method based on oil-indexed pricing with one that relies on hubs.

This is a major point of contention, especially for producers. The good news is that the issue is being discussed under a cooperative framework. However, the pace at which this is happening is not satisfactory to many consumers, who are mulling purchases of producing assets abroad or creating procurement consortia to try to bring gas prices down.

In recent discussions at the Asian Ministerial Energy Roundtable, two things about partnerships stood out. First, producers and consumers are already striking deals and cooperating closely. Technology and capital from Asia—a net gas consumer—supporting the output expansion in the Middle East region, which is a net producer, are a case in point, and a clear example of how embracing interdependence makes for good business and enhanced energy security.

Second, partnerships, which rely on trust, require more transparency when it comes to data sharing and the use of markets. Information like that provided by the Joint Organizations Data Initiative (JODI), which integrates production, consumption, exports, imports and inventory data from all corners of the world, can still be improved upon and made more broadly available with the cooperation of more governments and companies. But this depends on recognizing the important role that transparency plays in making markets work better.

There can be little doubt that partnerships will remain at the core of the industry. But they need clear rules for investment and the distribution of rents. They also must have the flexibility to cope with large sets of issues that may come up in the course of a project's investment cycle. Dialogue, mutual understanding, trust, and recognition of interdependence supported by transparency are key factors to sustain this type of partnerships and steer them in the right direction as circumstances change.