



# Impact of Low Crude Oil Price on Local Supply Chain and Recommended Mitigation Actions



## NIGERIAN CONTENT DEVELOPMENT & MONITORING BOARD

Directorate of Planning, Research and Statistics



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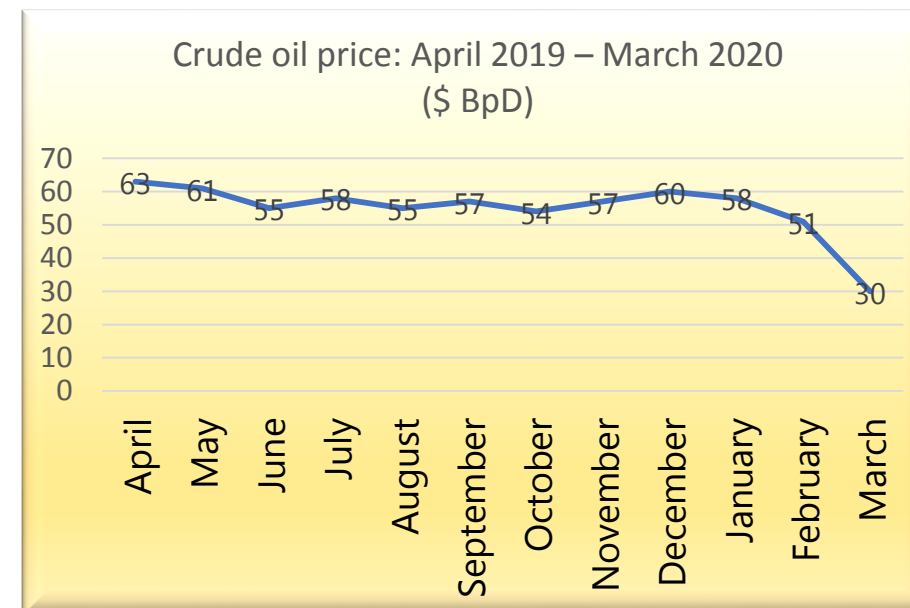
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# Introduction



1. The oil and gas industry is characterized by Bust and Boom cycles as it relates to pricing of the commodity
2. Typically contracts for procurement of goods and services are benchmarked against international price of crude oil.
3. During Boom period the industry witness significant growth in capacity, technology acquisition, training, employment and revenue due to good pricing for goods and services
4. During Burst period low pricing of goods and services lead to job loss, idle capacity, obsolete equipment and possible liquidation of some companies
5. The Nigerian Oil and Gas Industry is currently undergoing a Bust period with price of oil declining from \$63 per barrel in April 2019 to \$30 per barrel in March 2020
6. In view of the cyclical nature of crude oil pricing and its impact on the local supply chain the need to develop a sustainable business continuity plan during low oil price scenario has been identified
7. The overarching thrust driving the intervention is as follows:
  - a. Need to ensure business continuity and capital retention under Burst season
  - b. Need to sustain capacities established during the Boom period
  - c. Need to retain skills pool within the industry



Sources:  
<https://www.macrotrends.net/2516/wti-crude-oil-prices-10-year-daily-chart>

8. Key interventions being considered include:
  - a. Revenue Credit Scheme to mitigate potential loss in revenue and capital
  - b. Skills pool strategy to minimize loss of skilled manpower
  - c. Shared Services Model to contain cost and mitigate loss in capacity already established
9. Adoption of these interventions will ensure that current and future cycles of Burst do not impact adversely on the local supply chain and local content implementation

# Impact of Low Crude Oil Price .....



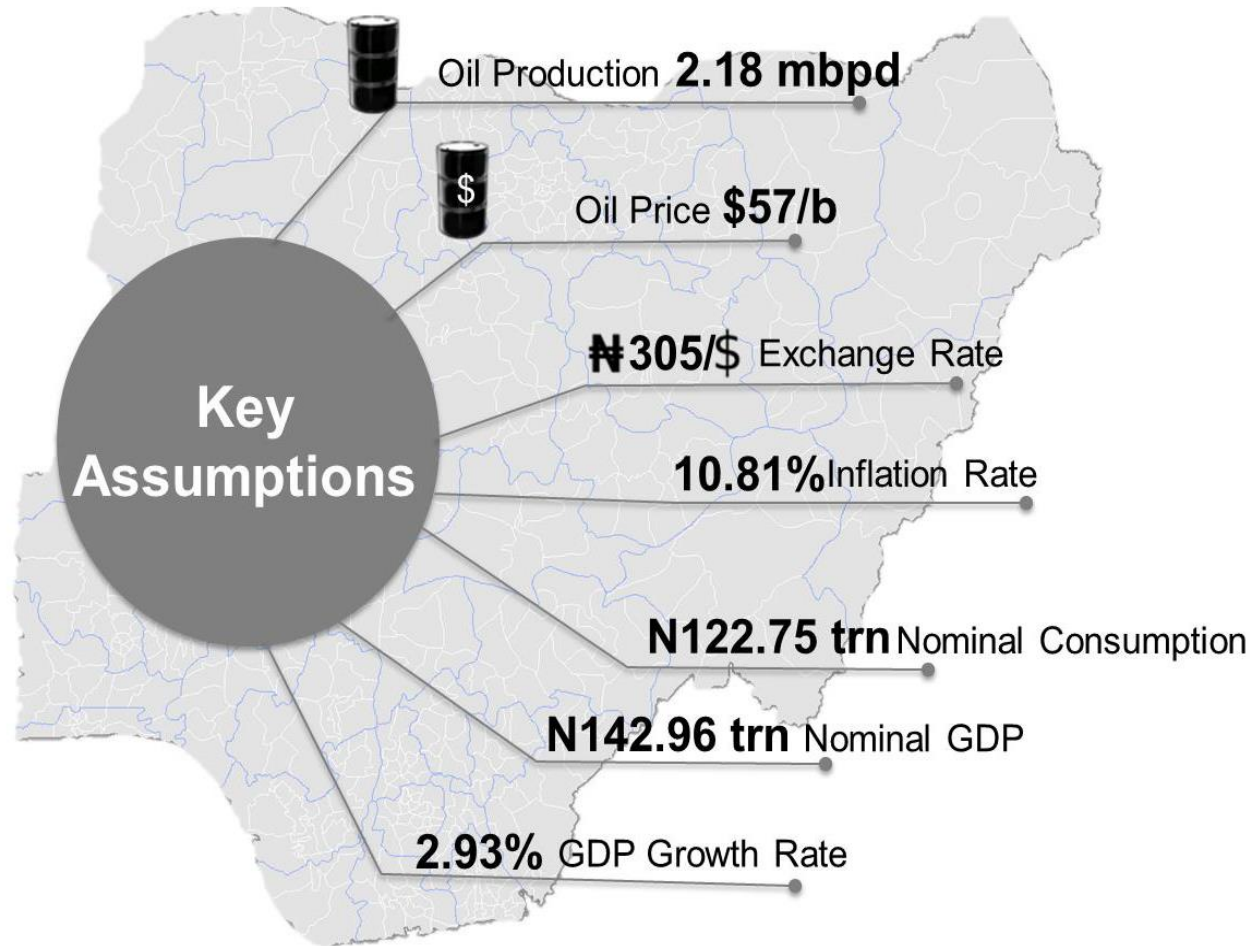
## **Government**

1. Drop in contribution of oil to Government revenue projection for 2020
2. Depletion of foreign reserves (from \$45 billion in April 2019 to \$35.52 billion in March 2020 )
3. Unemployment pressure (freeze on new employment)

## **Oil and Gas Industry**

1. Downward renegotiation of ongoing contracts
2. Suspension of new projects
3. Inclination to sacrifice local content .
4. Stunted growth in hydrocarbon reserves due to suspension of exploration activities

# Government ...Impact on 2020 Budget Framework



## 2020 budget assumptions

Adapted from Ministry of Finance highlight/Breakdown of the 2020 executive budget proposal

Approved 2020 budget **₦10.59trn**

1. Capital expenditure **₦2.46trn**
2. Recurrent expenditure **₦4.84trn**
3. Other expenditures **₦3.29trn**
4. Contribution from O & G **₦2.64trn**
5. Contribution from Non O&G, & debt **₦7.95trn**



## Revised

1. Prioritise growth- enhancing, pro- poor expenditure and social investment
2. Eliminate non critical capital expenditure- ICT, vehicles, building, furniture, training - exclude fire truck and security vehicles
3. Maintain personnel cost, suspend new recruitment
4. Reduce overhead by 16.7%
5. Reduce capital budget by 25%



# Impact on Government Revenue and Key Actions



## Impact

1. Drop in contribution of oil to Government 2020 revenue
2. Depletion of foreign reserves
3. Unemployment pressure



## Key Actions 1-2 years

1. Prioritize expenditure and recalibrate 2020 budget
2. Block revenue leakages and eliminate waste
3. Diversify economy to boost non oil revenue- Agriculture, Telecommunication, Solid Minerals, Manufacturing etc.
4. Focus on inward utilization of hydrocarbon resources – gas to power, LPG utilization, petrochemicals, refined products etc
5. Apply tax credit strategy to encourage participation of Corporates in infrastructure development
6. Deregulate downstream petroleum sector
7. Expand scope of local content to other sectors through legislation
8. Prioritize development of power, transport and telecommunications infrastructure to enhance local production

# Impact on Oil and Gas Industry and Key Actions



## Impact

1. Downward renegotiation of ongoing contracts
2. Suspension of new projects
3. Inclination to sacrifice local content
4. Stunted growth in hydrocarbon reserves due to suspension of exploration



## Key Actions 1-2 Years

1. Implement Revenue Credit Scheme for ongoing contracts to maintain sanctity of contracts, mitigate impact of contract renegotiation or suspension of contracts
2. Deploy shared services strategy to mitigate idle capacity
3. Accelerate targeted capacity building programs to enhance efficiency of local supply chain
4. Adopt skills pool model

# Impact on Service Companies – Reference PETAN Companies

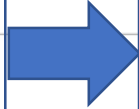


	Criteria	Cumulative Economic Value		
		US\$	Naira ₦	Number
1	Estimated value (\$) of Lost sales or income	2,033,940,944.00		
2	Estimated direct job losses (0-6 months)			14,082
	Estimated indirect job losses (0-6 months)			18,000
3	Estimated value (\$) of cancelled contracts	572,635,296.00		
4	No of staff employed by PETAN companies			23,814
5	Value of taxes paid by PETAN companies 2017-2019		36,880,750,000.00	
6	Value retained by PETAN companies in Nigeria			92%
7	Activities PETAN companies are involved			250
8	PETAN companies exposure to the banks (US\$)	186,078,533.52		
9	PETAN companies exposure to the banks (Naira)		123,040,350,864.00	
10	Value of corporate social responsibility of PETAN companies 2017-2019		5,126,561,489.55	
11	Value of Withholding Tax Deductions at Source 2017-2019		98,037,305,446.40	

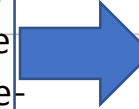
# Oil Contract Pricing Reality Check



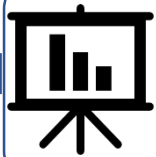
Theoretically, Contract Prices are based on Crude Price.



Nigerian Reality the Contract award is a Highly competitive process facilitated by NiPeX e-market platform



Number of Bidders invited to participate in a typical Nipex tender ranges from 10-1000+ companies



Generally, this means service companies price services to have competitive edge and deliver to desired quality



Implication is that bidders are not necessarily considering Oil price when bidding. Primary consideration is how to become the lowest bidder



Typically, after a highly competitive technical and Commercial process. Post Commercial, operators have the leverage to negotiate price with the lowest bidders



Therefore, Nigerian Oil and Gas contract prices are mostly a derivative of massive competitive forces



summarily, reduction in prices of already lean contracts by Operators during the periods of Oil price burst is potentially detrimental to service companies





# Risk Analysis: Downward Renegotiation of Ongoing Contracts



## Impact Area

1. Downward renegotiation of ongoing contract

## Responsibility

NCDMB/NNPC  
/Operators

## Mitigation and Benefits

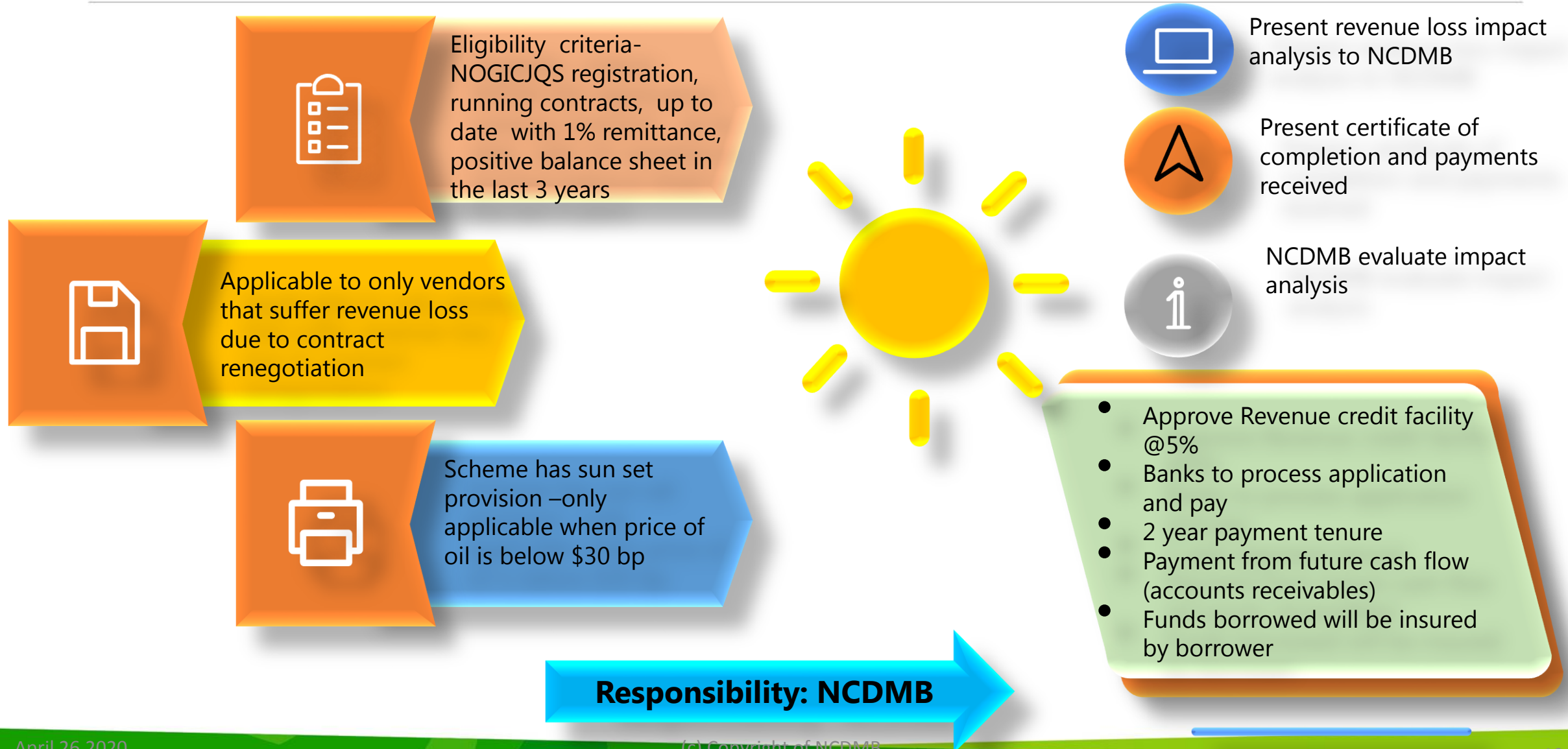
## Risk Analysis

1. Disruption of cash flow projection
2. Breach of contract terms
3. Default in loan obligations
4. Threat to acquisition of new technology
5. Relegation of investment in R&D
6. Skills mobility to other sectors due to job loss
7. Sub-optimal capacity utilisation and erosion of established capacity

## Revenue Credit Scheme Benefits

1. Sustain domiciliation activities
2. Invest in R&D and acquisition of new technology
3. Keep jobs
4. Retain and grow capacity
5. Access credit facility to augment revenue loss

# Revenue Credit Scheme





# Risk Analysis: Suspension of New Projects

## Risk Analysis

- Stretched business development cost
- Idle capacity
- Stunted growth in hydrocarbon reserves due to suspension in exploration

## 2. Suspension of new projects



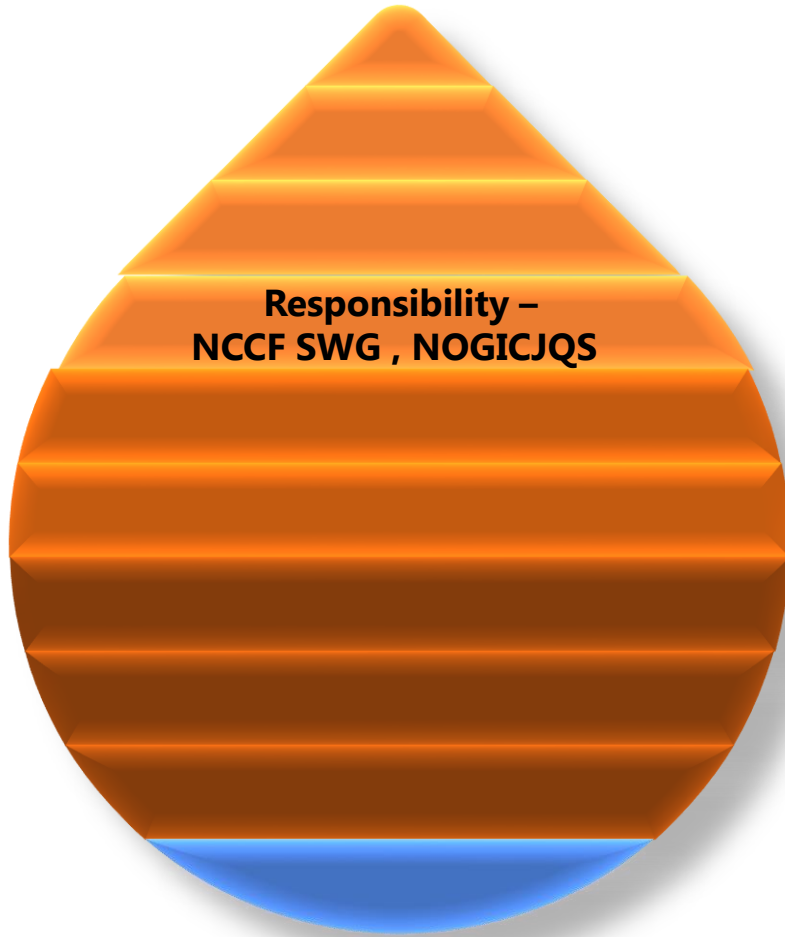
## Responsibility

MPR/NNPC/Operators

## Mitigation and Benefits

- Implement flexible fiscal policy to accelerate FID and exploration activities
- Develop efficient and competitive local supply chain
- Adopt shared services strategy and skills pool to manage cost across board

# Shared Services Strategy



## Key Actions



Develop data base of companies



Companies upload their Service Offerings



Companies share information on available assets - Equipment, facilities, logistics



Broadcast database of available assets and availability



Company(s) utilize available assets based on availability and demand

## Benefit

1. Reduce idle capacity
2. Optimize capacity utilisation
3. Promote alliance
4. Accelerate demand for space in NOGaPS sites





# Skills-Pool Model

Reduce mobility  
of labour

Benefits

Promote alliance  
among service  
companies

Reduce  
unemployment

Responsibility-  
NCCF SWGs

Key Actions

Develop data  
base of  
companies



Companies  
upload their  
service  
offering



Staff list and  
competencies  
uploaded



Broadcast database  
of available skills



1. Skill pool based on needs
2. Compensation based on utilization





# Risk Analysis: Inclination to Sacrifice Local Content



## Risk Analysis

1. Breach of NOGICD Act
2. Loss of confidence in sanctity of NOGICD Act
3. Zero investment in new capacities

## Mitigation and Benefits

A

Resist pressure to waive provisions of the NOGICD Act

B

Allocate space in NOGaPS site to attract OEMs

C

Invest in Capacity Building - training & infrastructure

Responsibility

NCDMB-PCAD  
/DPR/NNPC/Operator  
s/SON

**3. Inclination to sacrifice local content**



# Positive Outlook from Burst Season



No subsidy pay out-  
more income for Govt.



Reduction in environmental  
pollution and other emissions

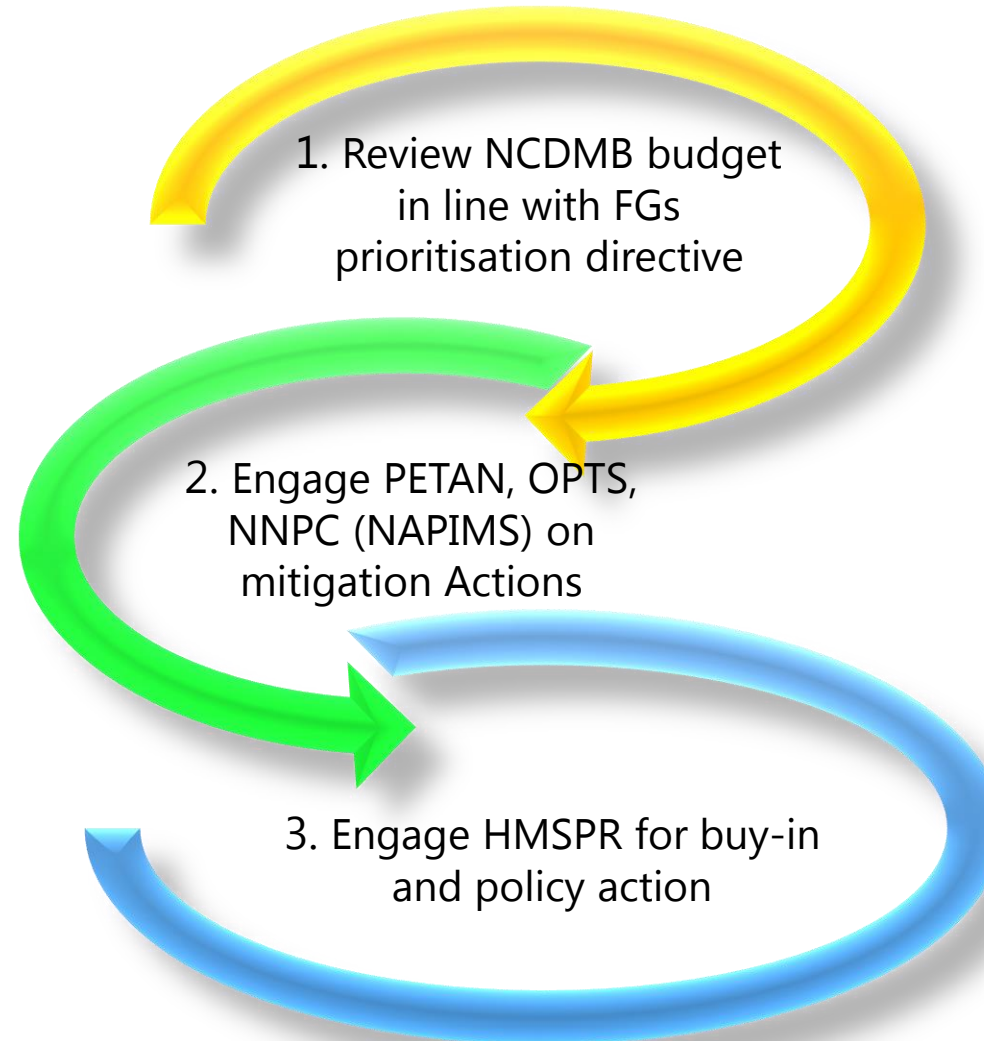


Economic diversification to  
drive non oil revenue



Suspension of new  
electricity tariff

# Next Steps





### **Research Team :**

Patrick Obah

Abdulmalik Halilu

Omomehin Silas Ajimijaye

Adeola Omole

Lilly Warri

Arikewuyo Umar Kayode