



North Sea prospects in challenging times

These have been challenging times for North Sea oil and gas operations, faced with the coronavirus pandemic and oil price collapse. Here, we examine the prospects for the UKCS and Norwegian sectors, and the impact on merger and acquisition deals, from leading analysts at Rystad Energy.

Last year was an anomaly given the COVID-19 pandemic and price collapse which affected the oil and gas industry severely,' remarks Sonya Boodoo, Vice President Upstream Research, Rystad Energy, in a detailed analysis of North Sea prospects, with fellow analyst Sara Sottillotta looking at the prospects for energy services.

Exploration activity was one of the hardest hit segments and many companies took the decision to reduce discretionary activity. At the beginning of 2021 the North Sea E&P industry was optimistic and anticipated that more than

20 exploration and appraisal wells would be completed. However, increasing numbers of companies deferred their exploration programmes. By the end of 2020 only eight wells had been completed.

The only discovery last year was the 120mn boe Isabella gas discovery in the Central North Sea. This year, the sentiment continues to be cautious and some companies, like Total, have deferred exploration activity till 2022 or later.

However, Rystad is cautiously optimistic and Boodoo believes: 'The forecast numbers are expected to increase slightly.'

CNOOC is expected to be one of the busiest explorers in the UK Continental Shelf (UKCS), with two appraisal wells on the recent Glengorm discovery, one of which was already completed, and a wildcat on the Shackleton prospect. Harbour Energy (formerly Chrysaor, before the reverse take-over of Premier earlier this year) is expected to drill two prospects, Talbot and Dunnotar. Shell will also be drilling the Jaws and cross-border Edinburgh prospects later this year, while Ithaca Energy (owned by Delek) will be drilling the Fotla prospect. Equinor recently spud the Tiger Lily prospect east of Shetland, and Serica Energy is eyeing North Eigg, with plans to drill in 2022, while Petrogas is expecting to drill Birgitta in the Central North Sea.

The Norwegian sector was more buoyant, yielding nearly 600mn boe in 2020. The two largest discoveries, with over 100mn boe each, are Slagugle and Warka. ConocoPhillips became the most active explorer on the Norwegian Continental Shelf (NCS) last year, operating three of the 14 discoveries, including the two largest finds. Neptune and Equinor also operated a significant share of discoveries.

Meanwhile, exploration performance on the NCS (in terms of volumes per discovery) was the highest in recent years, with 33 well bores aggregating 586mn boe – double what was seen in 2019, despite roughly 50% less wells being drilled. 'The latest well count points to strong activity comeback in 2021... with close to 50 wells likely to be completed by year end,' says Boodoo.

There is also indication of increased exploration expenditure, with 2021 budget levels comparing closely to 2019 levels. Both Lundin and Aker BP have indicated increased exploration budgets compared to 2020, and Equinor intends to drill 20–30 wells.

On the UKCS, exploration expenditure is likely to remain stable until 2023. Rystad Energy estimates total spend on the UKCS dipped by 20% in 2020 compared to 2019. Capex, excluding exploration activity, fell 27% and is expected to remain fairly stable until 2023. 'We see companies weighing their options before making final investment decisions. Considerations such as strengthening balance sheets, ESG [environmental, social and governance] target and offshore safety will remain high on the agenda,' notes Boodoo.

Pipeline of projects

A pipeline of projects is on the horizon to be sanctioned by 2025. In 2020, only two developments were approved – IOG's Core Project Phase 1

Projects west of Shetlands like BP's Clair South, part of the Clair Ridge project (pictured), will drive an uptick in capex in 2024

Photo: BP

and Wintershall's Sillimanite field – while Ithaca Energy submitted the Abigail field development for approval.

Rystad expects several projects to be approved in 2021. Tailwind Energy's Evelyn project has been greenlighted by the OGA, and Harbour Energy's Tolmount East is expected to be approved, as well as IOG's Core Project Phase 2 and Hibiscus Petroleum's Marigold. Repsol Sinopec's Tain project is anticipated to reach FID (final investment decision) this year. Most of these projects, with the exception of Marigold, are tie-back developments. Roughly 130mn boe is likely to be sanctioned in 2021.

As mentioned, many expected projects have been delayed, including Siccar Point's Cambo development west of Shetland. Rystad expects sanctioning in 2022, as Siccar Point is trying to farm-out its interests prior to FID.

Projects west of Shetland will be driving the uptick in capex in 2024 and beyond, with Cambo, BP's Clair South and Rosebank on the horizon. Development activity is likely to surpass 2020 levels but not rebound to 2019 levels.

Drilling activity also slumped by 42% in 2020, with only 65 development wells drilled, compared to 112 in 2019. Some 23 wells had been spudded by June 2021, with another 31 awaiting approval from the OGA. It is anticipated that development wells in 2021 will surpass 2020 levels. OGUK expects around 70–80 development wells to be drilled this year.

In 2020, there was a 5% reduction in overall production, as a result of deferred activity and maintenance. A further 3.5% decline in output is expected in 2021, with production of about 1.5mn boe/d in 2021.

On the Norwegian side, development activity was expected to falter a bit, with many operators announcing delays for projects previously expected to be sanctioned in 2020. However, the Norwegian government implemented a temporary tax regime to mitigate the effects of this. The breakeven price under the temporary tax regime

is on average around 40% lower than the main regime. AkerBP, for example, reported around \$8/boe reduction and Lundin around \$10/boe reduction and their IRR (internal rate of return) doubled.

Prior to the announcement of the temporary tax regime, only one project – Balder X – was approved in 2020. With the introduction of the new tax regime, four projects gained approval in 2021, and 2022 is expected to be a very active year with an all-time high in projects being sanctioned. Aker BP is targeting around 550mn boe in the next two years, and Lundin is eyeing about nine potential new projects with about 200mn boe to be sanctioned by 2022.

Rystad expects capex on the NCS to remain relatively stable at around Nkr150bn (\$17.44bn) until 2025 under the temporary tax regime and fixed price assumption. However, without the temporary tax regime, there could be a significant drop in capex, because of lack of an incentive to sanction within that time.

M&A activity

Given the uncertain price environment encountered last year, it was not surprising that the level of M&A activity took a dip in 2020, 'as buyers and sellers found it difficult to navigate the bid/ask price,' says Boodoo. Roughly \$2bn in assets was traded in the UK in 2020, down from \$6bn in 2019.

The largest deals in 2020 involved Viaro Energy acquiring RockRose Energy for £248mn and SSE gas and exploration assets for £120mn. Transaction activity picked up pace in 2021 with the improved price environment. Enquest acquired interests in the CNOOC-operated Golden Eagle field from Suncor in a \$325mn deal. NEO Energy acquired a package of non-operated UK upstream assets from ExxonMobil (seven months after it bought a clutch of Total assets) and also Zennor Petroleum's portfolio for \$1bn and \$625mn respectively. NEO Energy expects to triple its oil and gas output to 100,000 boe/d in 2022–2026 on the back of the acquisitions. Meanwhile, Cairn Energy sold its minority stakes in Premier's Catcher and Enquest's Kraken fields to newcomer Waldorf Production for \$420mn.

'It is likely that continued M&A activity will be on the agenda and many portfolios are on offer,' comments Boodoo. 'One factor that drives transaction activity in the UK is tax synergies. A substantial number of companies, such as Enquest, Equinor, Cairn and Ithaca have significant tax losses to be utilised. Acquiring portfolios with

production could accelerate the utilisation of these losses, adding additional value.' This trend was seen as a significant value add in the Golden Eagle transaction earlier this year, as well as the major Chrysaor/Premier merger last year.

'The flurry of M&A activity in the UK provides some much-needed optimism for the future. The new owners of these fields will be eager to push forward with incremental development and also progress development of new fields to maximise the UKCS potential,' says Boodoo.

On the Norwegian side, there have been some interesting M&A deals as well, both with large corporate deals like PGNiG's acquisition of Ineos Norway and Longboat Energy's entry on the NCS through a mixed portfolio acquisition, and smaller single asset and licence acquisitions like Lime Petroleum's acquisition of Repsol's stake in the Brage field. Rystad expects more transactions potentially to come in the light of Shell's public statements of plans for an exit from the NCS. Shell currently has a strong position on the NCS, with the Troll and Ormen Lange fields being the largest contributor. Boodoo notes that a significant part of the Shell NCS portfolio is electrified, and divesting it seems somewhat counter-intuitive in terms of achieving their carbon emissions target.

Oilfield services slump

Analyst Sara Sottolotta notes that European upstream investments were running 14% lower than 2019 levels in 1Q2021. The pandemic erased \$19bn in purchases of oilfield services in north-west Europe. 'Engineering expenditure is reeling and sanctioning activity has slowed in the North Sea,' she says. According to Rystad calculations, engineering performance, construction and installation in 2020 suffered a \$2.5bn drop (30% fall) compared to 2018, due to decrease in activity.

Offshore service prices dropped by 12% on average from 2019 to 2021. The subsea market is expected to be one of the key drivers of price inflation in the North Sea from 2022 onwards.

North Sea expenditure is expected to remain flat in expectation of new contract awards of about \$50bn – mostly in Norway (\$29bn) and up to \$17bn in the UKCS and others, with a 'spending spree' anticipated in 2024. 'We expect sanctioning activity in the North Sea to make a serious comeback in 2022, mostly driven by offshore activity,' says Sottolotta. So there is something to look forward to. ●

One of the largest deals in 2020 involved Viaro Energy's acquisition of RockRose Energy for £248mn; assets included the Blake and Ross fields in the central North Sea (pictured here being serviced by the Bleo Holm FPSO)

Photo: Viaro Energy

