SHARKS IN THE WATER

ENVERUS Drillinginfo

WHITE PAPER

"DICE ARE ROLLING, THE KNIVES ARE OUT..."

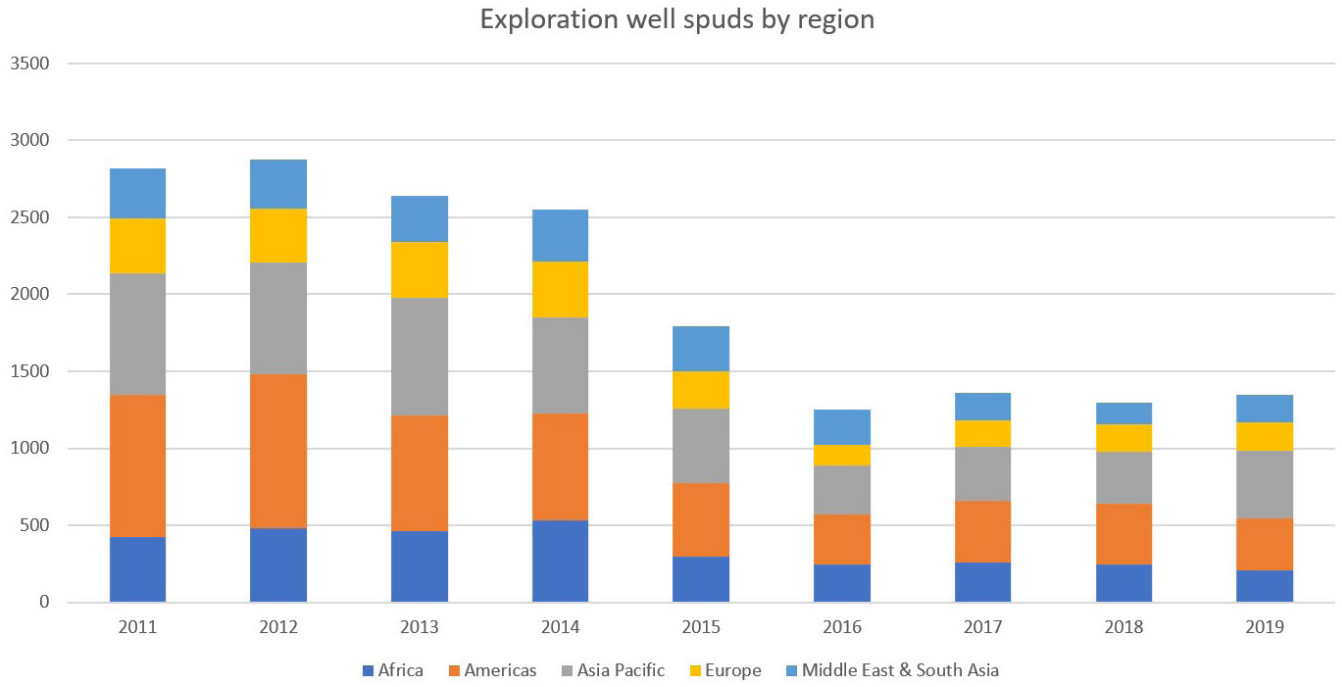
Oil's recent price implosion, resulting from the double whammy of OPEC's early March failure to agree on further production cuts with Russia and demand destruction in the wake of the global coronavirus pandemic, has left the global oil and gas exploration business reeling. Subsequent OPEC++ cuts announced on Easter Sunday did not exactly bring much relief in the near term. They are unlikely to keep up with plunging demand – thought to be down as much as 20 million barrels of oil per day or more – and uncertainty will likely continue to plague the industry. Companies weakened by what were already low commodity prices and huge debt costs are now fighting to survive. Not all of them will.

In this series we'll highlight not those about to be eaten, however, but rather the sharks in the water: companies with solid balance sheets, long-term growth strategies, and cash to spend on acquisitions from stressed rivals.

With the belief that oil prices must rebound – eventually – these stronger companies are already filling their coffers by selling debt, allowing them to go shopping with that relatively cheap money rather than using proceeds from farmouts and divestments. ExxonMobil took advantage of the recent rate cut and raised cash after canceling its US GOM divestment program. Equinor raised $5 billion in early April through debt offerings and further bolstered its cash reserves by canceling share buybacks and slashing various investments, including US onshore drilling programs. BP, Total, Shell, and even Austria's OMV also raised money similarly in the last few weeks. But for companies with less robust balance sheets, debt will not be an option, and many will be forced to sell assets at unfavorably low prices to those who simply have bigger teeth.

We anticipate a continued increase in the Asia Pacific region's share of exploration activity, at the expense of the Americas and Europe (**Figure 1**). Opportunistic buying will similarly concentrate in the Asia Pacific and Africa regions, driven by a combination of hydrocarbon-friendly regimes, reasonable political stability, local demand growth, and recent discovery trends.

FIGURE 1 - Exploration Well Spuds by Region 2011-2019



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For our company-by-company analysis, we've broken our shiver of sharks into four main categories: supermajors, large independents, NOCs/ex-NOCs, and others. We'll begin by focusing on a handful of supermajors we see potentially leading the way, starting with Shell.

SHELL

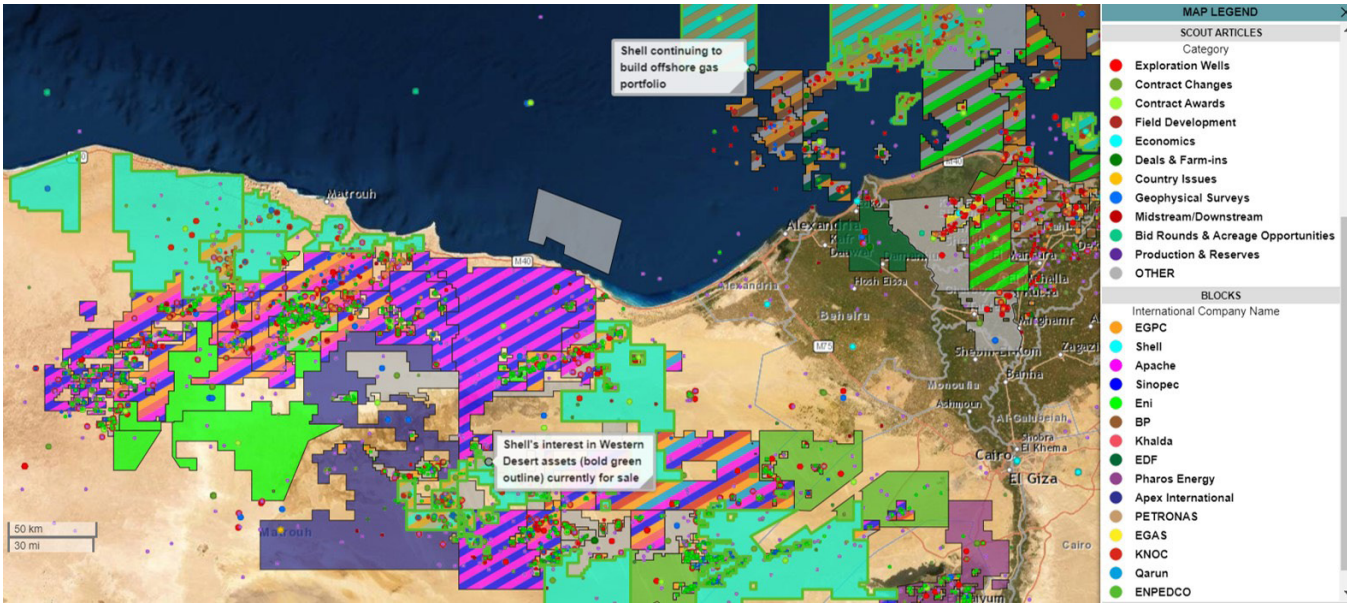
Shell's financial strength and consistent appetite for costly but profitable exploration should have it on the hunt. In Brunei, where the company is literally part of the history of oil and gas development, Shell picked up Total's operatorship in Block CA-1 in early April 2020.
The block is located southwest of Total's Tepat 1 discovery well in Malaysia's Baram Delta Basin Deepwater Block N. The Tepat 1, which was plugged and abandoned in March 2018, may have encountered up to 100 meters of gas and 50 meters of heavy oil potentially within the "Cycle II" Upper Oligocene-Lower Miocene carbonate reservoir and caught Shell's expert eye as indicative of new regional potential. Look for Shell to continue building its position here.

In the eastern Arabian peninsula, where it has a longstanding exploration history, Shell and non-operated partner Total (25%) are still awaiting ratification of their 2018 awards in Oman's Greater Barik area, pending finalization of an Exploration and Production Sharing Agreement (EPSA). Focusing on gas development, the four blocks (10/10B/11/11B) total 4,010 square kilometers and lie largely in the Ghaba Salt Basin, where Shell-managed PDO encountered gas in several exploration wells over the last 30 years.

As well, Shell in October 2019 was awarded 100% interest in Block 55 (Kahil) in the South Oman Salt Basin, following the block's relinquishment by Petrogas a year and a half earlier following three unsuccessful exploration wells. Under the terms of Shell's agreement, total investment in the block will be around US$ 65 million in G&G studies, seismic acquisition, and exploration drilling, with oil the main target. Shell seems to have plenty to do in Oman at the moment and is unlikely to tack on more assets any time soon.

In October 2019, Shell announced its intent to sell its entire Egypt Western Desert asset base (**Figure 2**). As of mid-April 2020, one international consortium and an Egyptian entity were said to have been invited to join the second round of bidding. The asset sale was flagged by Shell as part of a strategic re-focus on its offshore gas activities in the Egyptian Mediterranean (western Nile Delta), where the company has been carrying out an approximately US$ 1 billion exploration and development drilling program and where we think any additional African acquisitions by Shell are most likely to occur.

FIGURE 2 - Shell Western Desert and West Nile Offshore Blocks, Egypt



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Finally, Shell must be looking at ways to replenish its reserves in northern Europe, where it sold a large package of UK continental shelf (UKCS) assets to Chrysaor in 2017 and faces additional reserves write-offs at Groningen field, where the Dutch government ordered gas production to end in 2022 because of induced seismicity. Though it has been fairly conservative in Norway and the UK in the last few years, Shell's likely acquisition targets lie in the Norwegian Sea and West of Shetland (near Schiehallion and Clare fields), where it has remained relatively keen.

TOTAL

We see Total as an apex predator, a great white among the sharks, likely eyeing Latin America, Africa, and possibly central Europe for opportunistic expansion.

Total is a world leader in natural gas, with massive reserves and a significant stake in the global LNG business. Brazil is in the early stages of a massive gas supply transition, with Petrobras being stripped of its gas monopoly and pre-salt production continuing to come online. Gas use in Brazil's energy mix is growing, though it lags many other countries in the region. With the country committed to reducing its carbon footprint, we see natural gas gradually replacing coal on a large scale, along with renewables. The country's gas pipeline and distribution networks remain relatively weak, but over the medium and long term that will change. New pipelines are already being built to move the huge quantities of pre-salt associated gas ashore (despite some of it having high levels of CO2), and as a result Bolivian gas imports have been significantly cut back in recent long-term contracts.

We expect Total to play a key role in the expansion of Brazil's gas market as a producer and possibly exporter over the long and medium term – and thus to be on the hunt for assets across the value chain. Although the company recently canceled a Brazil drilling rig contract, this seems less of a retreat than a temporary balance sheet move, and we fully expect the company will continue to patiently await the right conditions. With less scrutiny and pressure on quarterly results than most companies, Total is well positioned to take on more oil assets in the country.

In Argentina, although we see no signs that Total wish to expand aggressively, we'd expect the firm to maintain its foothold, especially if the gas market remains profitable. Trinidad & Tobago, Guyana, and Suriname are also places where Total could pick up additional assets.

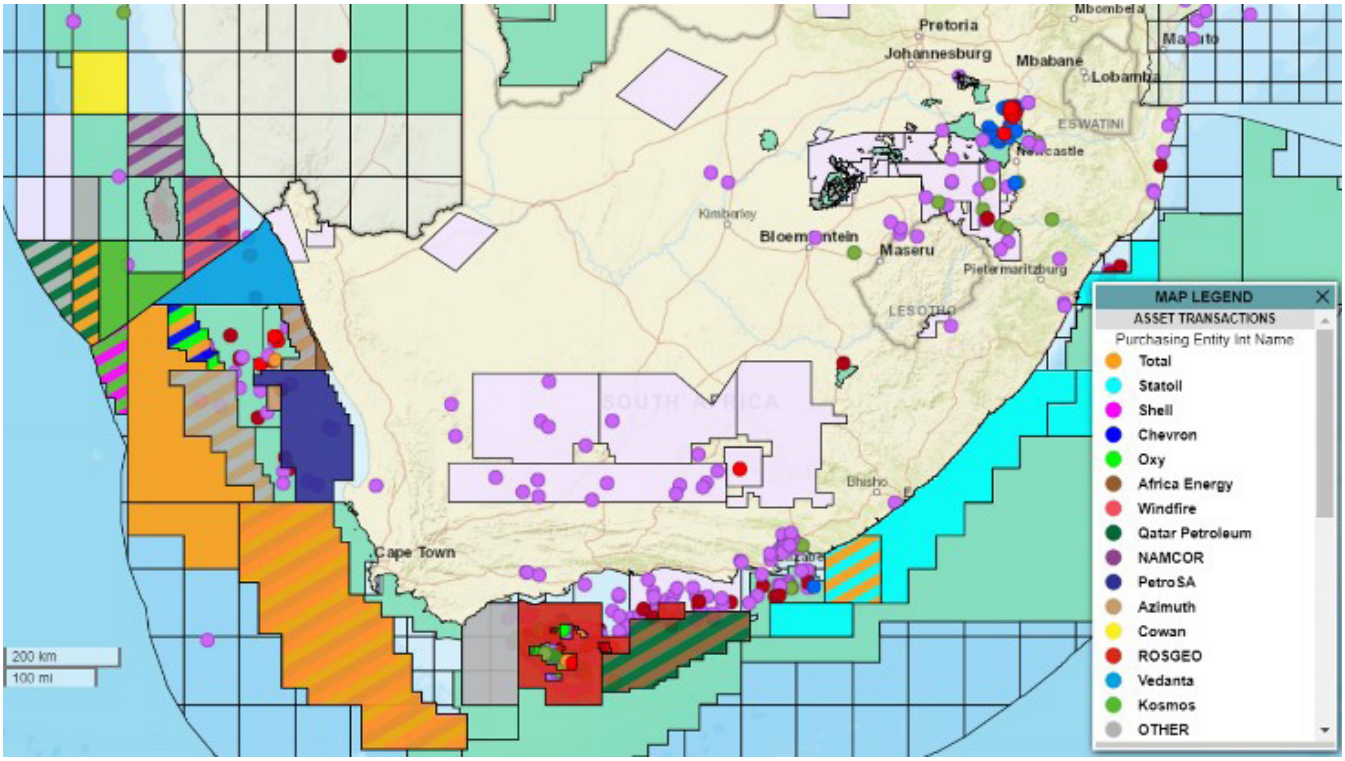
Before the oil price plunge, Total was likely considering a piece of the action in Nicaragua's Pacific offshore Sandino Basin, where Equinor operates nearly 16,000 square kilometers in Blocks C1, C2, C3, and C4. The Norwegian flagship explorer desperately needs a new partner for its planned Mango 1 exploration well following Cairn Energy's withdrawal from the blocks, but Total's exploration management may have a hard time convincing board-room players and bean-counting investors to deploy dry powder on the oily exploration play now.

In Africa, Total has been the biggest buyer of assets since the last downturn, with more than $19 billion in completed and pending transactions over the last five years, adding interests in over 300,000 square kilometers to the company's portfolio, notably in South Africa, Libya, and Kenya (**Figures 3** and **4**). Most recently, Total agreed to purchase all of Tullow's Ugandan interests for up to $575 million in a deal announced in late April. In Mozambique, Total has its hands full with the assets it acquired from Occidental (through its purchase of Anadarko) in 3Q19. It now operates Rovuma Offshore Area 1, where plenty of work lies ahead on the LNG development project, with local reports suggesting that Total is currently maintaining a 2024 target for first gas. However, uncertainties associated with the coronavirus and a rising threat level of Islamist militant activity in the Cabo Delgado region may disrupt the LNG project.

FIGURE 3 - Top Five Acquirers of Africa Blocks, Last Five Years (By Square Kilometers - Gross)

Source | Enverus International

FIGURE 4 - Southern Africa Block Acquisitions, Last Five Years



Source | Enverus International

Given the amount of work and current risks, one might assume that Total would maintain, rather than grow, its strategic position here, but we think the French supermajor has a big enough appetite to join in Mozambique's 6th Licensing Round (whenever it actually goes ahead) in an effort to match Eni's and Exxon's exploration presence in the offshore Zambezi Delta region.

Total will be focusing on the next exploration phase in South Africa's Outeniqua Basin after its play-opening Brulpadda wet gas discovery in 2019. Already in possession of 140,000 net square kilometers offshore Namibia and along South Africa's west and south coasts, Total's future expansion in South Africa will likely be along the east coast. The company tipped its hand late last year by picking up Equinor's 30% interest in the East Algoa block, Total's first move east of Block 11B/12B. Our second bet for southern Africa growth is in the Orange Basin, where the firm's Venus 1 new field wildcat is planned for summer 2020. With farm-in opportunities in the basin on both sides of the border, Total will try to build a dominant presence in the region if the well is a significant discovery.

In the Middle East, Total is still awaiting ratification of its 2018 awards in Oman's Greater Barik area, focusing on gas development with operating partner Shell (75%). In March 2020, Total and non-operator PTTEP were also awarded the adjacent Block 12 for the development of (non-associated) gas. These exploration projects, along with Total's partnership in Oman LNG, which already operates a plant in Qalhat and intends to build another to offer a bunkering service supplying LNG as fuel to marine vessels, have us thinking that Total's plate here is full.

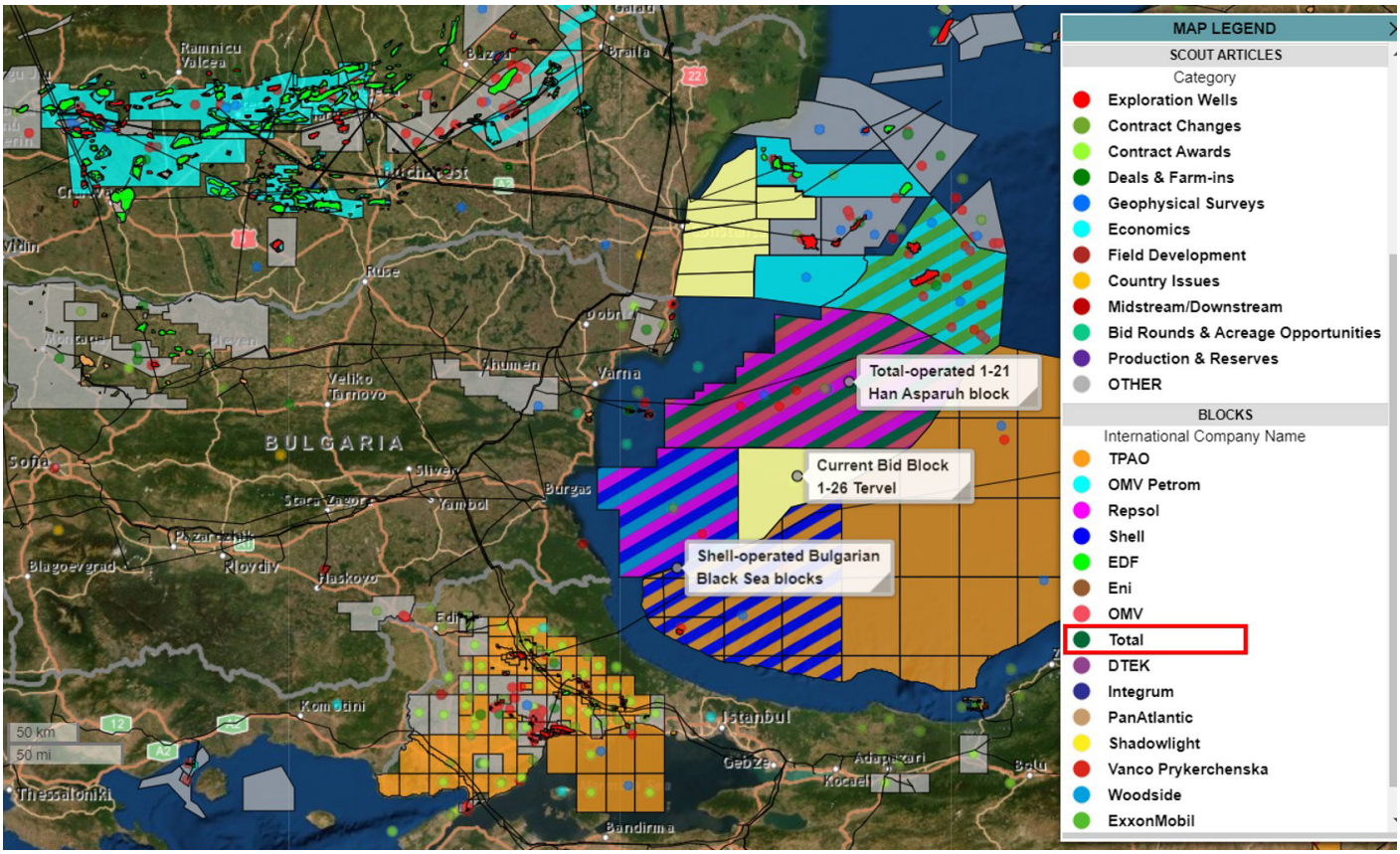
Lebanon might be a different story if Total is sufficiently encouraged by the recent results of its 16/1 new-field wildcat, the country's first-ever offshore exploration well. Drilled in Block 4, the well was reported in the last week of April to have encountered traces of gas, confirming the presence of a hydrocarbon system, but no reservoir in the objective Tamar formation. A second exploratory well, now due to be drilled in 2021 on Block 9 to the south and quite near Israel's Karish field, may hold greater promise due to its more proximal location to the Nile Delta, the source of the Tamar sands.

With Lebanon in a financial crisis even before the coronavirus outbreak, local economic and political considerations will factor into any decisions to expand here. Total operates both existing blocks in Lebanon, limiting options for acquiring more acreage to the recently extended second offshore bid round, now scheduled to close on June 1, 2020.

Having already given up most of its southeast Asia and Australia exploration acreage and trimmed the Singapore-based new ventures team and relocated the remnant to France, Total's gaze in Australasia is, in our belief, quite narrowly fixed on Papua New Guinea, where LNG is the play – firmly in line with the company's global strategy. Given the regional cuts and since Total's last acquisition in the area was three years ago, we simply don't see the region as the prey this shark prefers.

Lastly, with favorable fiscal terms and access to the attractive central Europe market, Total may try to expand its presence in Bulgaria (**Figure 5**), where it holds the 1-21 Han Asparuh license and seems prepared to persevere in spite of mixed drilling results to date (one technical success and two dry wells) that likely underlie rumors that Repsol will withdraw from the block . With a tender up for adjoining deepwater Block 1-26 Tervel, south of Han Asparuh and east of Shell-operated Han Kubrat, we'll soon see whether Total has an appetite for further Bulgarian exploration. If the company wishes to expand more broadly in the Black Sea, perhaps more likely targets are the upcoming (but serially delayed) Romania and seemingly more firm Ukraine tenders, with at least eight blocks between them. There was talk that Total was considering a bid for ExxonMobil's 50% share in the Neptun Deep project in Romania, although now it seems that a joint bid from Romgaz, PGNiG and OMV Petrom is favored. If Total views the Black Sea as geologically favorable to exploration and the central/eastern Europe market as more stable in the longer term, it may favor establishing an exploration position now rather than paying a premium for more proven resources later.

FIGURE 5 - Black Sea Blocks Under Contract and Open for Bidding



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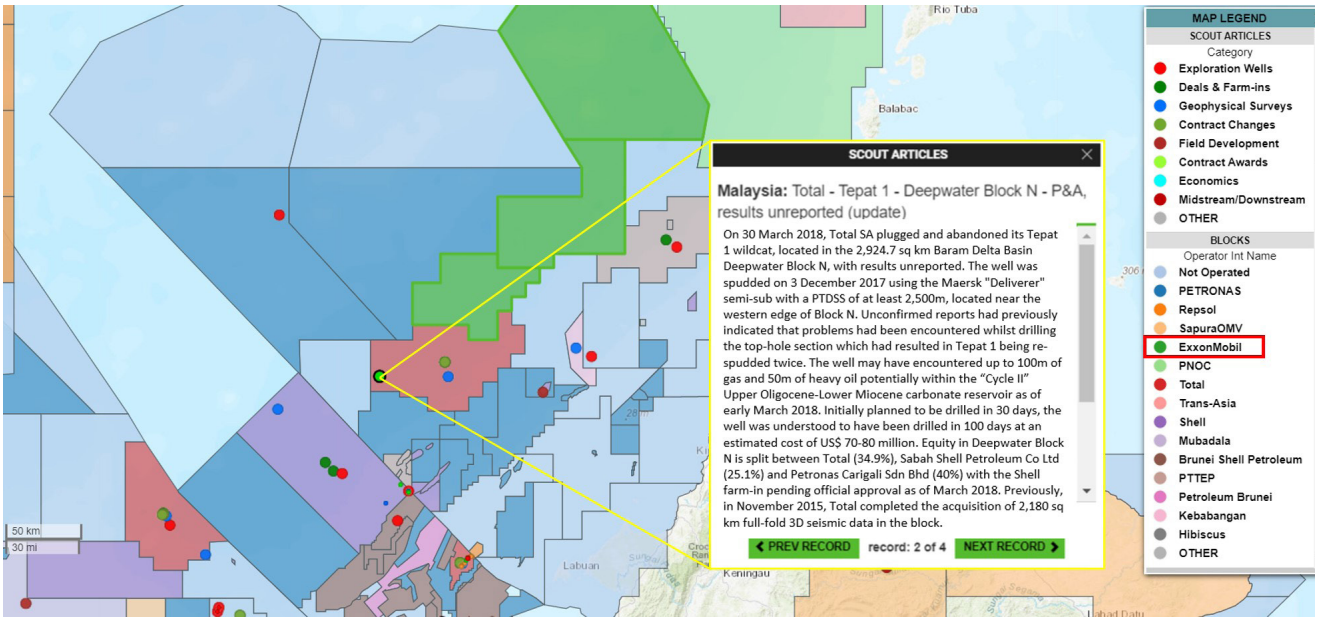
EXXONMOBIL

With Guyana-Suriname now firmly established as a world-class, likely multi-billion-barrel oil discovery, ExxonMobil will be peering into the future and considering where to place its next bets. Will its crystal ball portend a world in which oil demand has suffered a permanent decrease as a result of pandemic-related economic slowdown and concomitant opportunistic government policy lurches favoring renewable energy sources? This might incline ExxonMobil toward further expansion of its global natural gas and LNG business. Or will the crystal ball reveal a return to business as usual, with all energy sources and thus all hydrocarbon phases on the table?

We believe that ExxonMobil, although perhaps not thinking green quite as publicly as BP CEO Bernard Looney, sees a strong future in natural gas projects. One example is the company's far-sighted effort to establish a system of transportation infrastructure to expand gas access in India. Dubbed "virtual pipelines," the systems will deliver liquefied natural gas by road, rail and waterways to areas not connected by physical pipelines. This forward-looking gas focus would seem to be contradicted by ExxonMobil's proven reserves, which totaled 24.3 billion oil-equivalent barrels at year-end 2018, of which liquids represented 64% – up from 57% a year earlier thanks largely to Guyana, Brazil, and the Permian Basin (Texas). However, we see no signs that the company will work overly hard to shift the commodity mix of its exploration portfolio, more likely allowing the sale of older oil assets to shift overall reserves back toward natural gas.

ExxonMobil is actively marketing its production assets in west Malaysia, but in late 2017 and early 2018, it was awarded three deepwater blocks in east Malaysia's Sabah, one directly adjacent to Total's Tepat 1 well and the others extending northeast from there (**Figure 6**). Rumor has it ExxonMobil is still actively looking to expand in east Malaysia, presumably in Sabah and Sarawak. The recent installation of a new upstream business development leader in Singapore adds further intrigue to these rumors.

FIGURE 6 - Brunei/East Malaysia Exploration Blocks, with Tepat 1 Discovery Well Article



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Barring a significant course change, ExxonMobil's position in the Australia upstream sector is likely to continue diminishing. The firm's last acquisition came three years ago when it picked up all of Liberty Petroleum's interest in the 2,062-square-kilometer Block VIC/P70 in the Gippsland Basin. Now ExxonMobil's 50% interest in its BHP-operated Gippsland assets is for sale. Given this backdrop, it seems unlikely the company would have put in bids on the most recent Australia Offshore Petroleum Acreage Release. Neighboring Papua New Guinea, although certainly a significant ExxonMobil asset, also seems an unlikely locale for growth.

Carefully placing its bets in the Middle East, ExxonMobil didn't garner acreage in recent bid rounds in Lebanon, Israel, Iraq, Oman, and the UAE. However, it recently expanded in the Eastern Mediterranean by picking up blocks in Egypt that complement its acreage offshore Cyprus. And like its supermajor brethren, ExxonMobil will certainly be interested if and when Qatar decides to choose partners for its expansion of the North Field mega-project.

ExxonMobil has been steadily expanding its footprint offshore Africa over the last two years in Egypt, Ghana, Angola, and Namibia, and in the Sao Tome and Principe-Nigeria Joint Development Zone (with Total) and always seems to be ready for more.

Finally, at the top of its shopping list in the Latin America/Caribbean neighborhood is Trinidad and Tobago, where ExxonMobil will be looking hard at the planned 3Q20 deepwater bidding round, which holds the potential of oil and should appeal due to its potential scale and proximity to the supermajor's Guyana assets.

ENI

As for Eni, the only aspect of its giant Perla field that might still be appealing at this point is that it is natural gas. Offshore Venezuela and touted ten years ago as evidence of Eni's return to world-class explorer status, Perla's shine has been badly tarnished by its financially beleaguered host country resorting to payment in kind for production from the field, with oil cargos making their way slowly to Europe instead of dollars flowing quickly into corporate coffers. Coupled with the seemingly never-ending turmoil in Venezuela's economy and government and the ensuing chronic uncertainty in fiscal terms, surely Eni must be wondering where it can plant a flag in an easier Latin American asset.

One option in this vein might be the Walton Morant license, offshore Jamaica, where operator Tullow and partner United Oil & Gas are said to continue seeking partners for an exploration well on their Colibri prospect (**Figure 7**). Facing a July 2020 relinquishment of the blocks, however, an outright divestment of the asset seems more likely. Embattled Tullow is reported to have completely written off the acreage following a portfolio review that prioritized free cash flow and debt reduction, hence near-field opportunities in proven basins and earlier farm-downs of working interest in frontier exploration areas. This sounds like a large-and-tasty-but-injured target for shark-minded exploration management, although the Eni board room and investors may be feeling somewhat more cautious and prefer smaller fry.

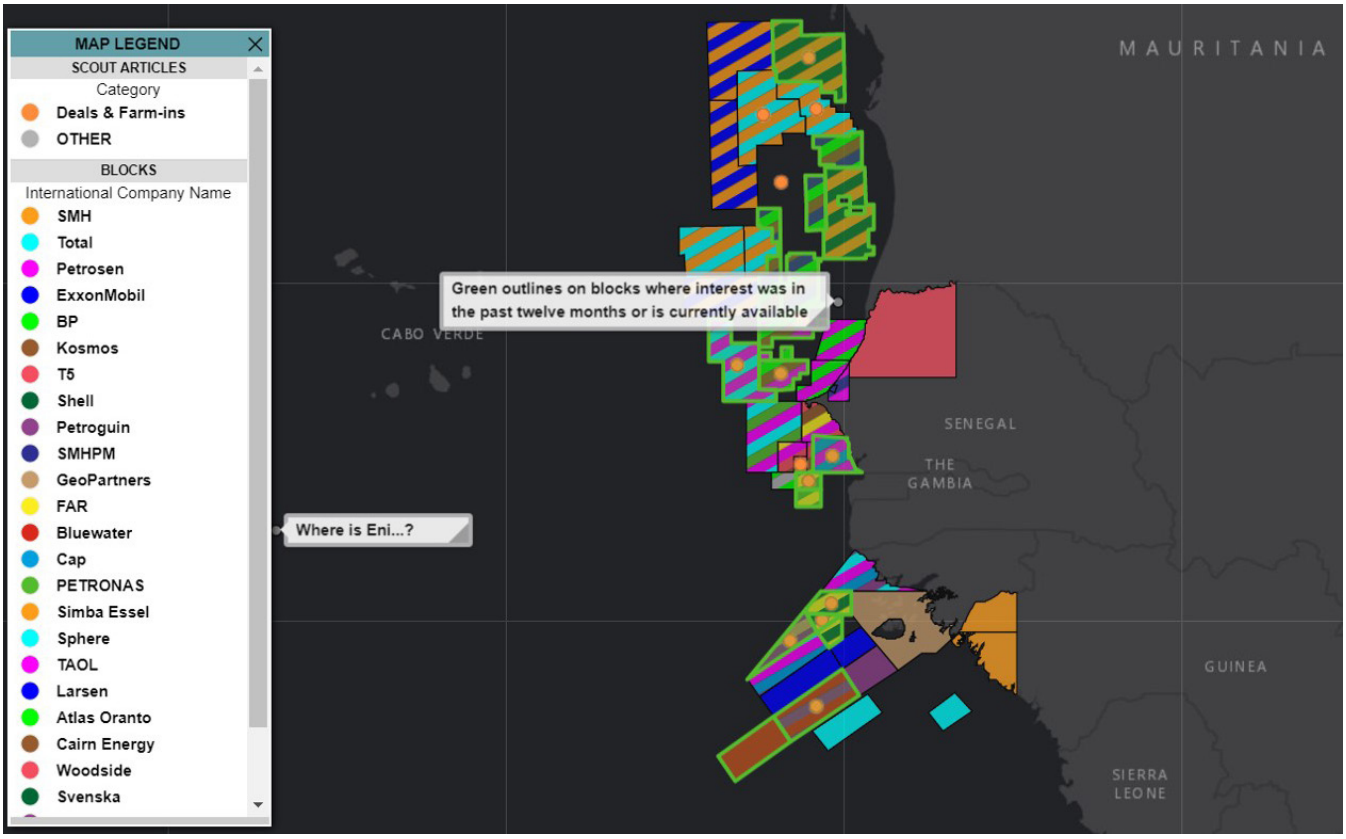
FIGURE 7 - Jamaica's Walton Morant License

Source | Enverus International

If Eni wants to expand exploration in Europe, it will have to look outside Italy, which has imposed a moratorium that will likely result in a reduction of company acreage there. A logical alternative for growth would be to continue leveraging its Mediterranean carbonate expertise and success, as it has already done by securing acreage in Montenegro and Albania. And in the North Sea Eni is pursuing growth through Vår Energi, its Norwegian JV with HitecVision, which is understood to be seeking expansion into the UKCS.

As for Africa, Eni maintains stakes in two giant gas projects: Zohr in Egypt and Rovuma Offshore in Mozambique. We would not be surprised to see the company make more strategic gas acquisitions via the future Angola bid rounds, the Mozambique sixth bid round, and possibly the next Ghana and Senegal bid rounds. But the elephant in the room is the MSGBC Basin, where Eni is arguably the largest company with no current upstream footprint (**Figure 8**). Either currently or in the past twelve months, considerable operated and non-operated interest has been available from numerous operators, including Shell (Mauritania C-10, C-19), Kosmos (six blocks in Mauritania and Senegal), Total (Senegal UDO-North), TAOL (Senegal Djiffere Offshore), FAR (Gambia A-2, A-5), Svenska (Guinea-Bissau 2, 4A, 5A), Geopartners (Guinea-Bissau 4B), and Supernova (Guinea-Bissau 7B, 7C).

FIGURE 8 - MSGBC Basin Blocks, Highlighting Interest Available Over Last Twelve Months



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SHARKS IN THE WATER

What do you think? Whom would you see as the predators if a feeding frenzy ensues? What have we missed or gotten wrong in your opinion? Fancy a look at our just-released Q1 activity maps? Our team of 27 international scouts, boasting over 400 combined years of experience, are willing and eager to engage with customers – and future customers – on these topics and more!

Lastly, stay tuned for the next installations of Sharks in the Water, in which we'll give you our take on the large independent E&Ps with large dorsal fins – and publish our thoughts on who takes out mortally wounded Tullow in the very near future.

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