

Ambitious Oil Sector Plans

Iran is the Organization of Petroleum Exporting Countries (OPEC)'s second largest oil producer and holds over 10 percent of the world's proven oil reserves. It also has the world's second largest natural gas reserves (after Russia).

Iran's economy, which relies heavily on oil export revenues (around 80 percent of total export earnings, 40-50 percent of the government budget, and 10-20 percent of GDP), was hit hard by the plunge in oil prices during 1998 and early 1999, but with the recovery in oil prices since then, has bounced back to a great extent. For 2003, Iran's real GDP grew by around

Attraction and Protection of Foreign Investment, which aims at encouraging foreign investment by streamlining procedures, guaranteeing profit repatriation, and more.

Resources

According to the Oil and Gas Journal (1/1/04), Iran holds 125.8 billion barrels of proven oil reserves, roughly 10 percent of the world's total, up from 90 billion barrels in 2003.

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that Iran could increase its crude oil production capacity significantly. Iran produced 6 million bbl/d of crude oil in 1974, but has not surpassed 3.9 million bbl/d on an annual basis since the 1978/79 Islamic Revolution. During the 1980s, it is believed that Iran maintained production levels at some older fields only by using methods, which have permanently damaged the fields. Despite

1.4 percent sulphur); Iranian Heavy (31° API, 1.7 percent sulphur); Lavan Blend (34°-35° API, 1.8 percent-2 percent sulphur); and Foroozan Blend/Sirri (29-31° API). Iran is also the largest heavy fuel oil exporter in the Middle East.

The domestic oil consumption, 1.4 million bbl/d in 2003, is increasing rapidly as the economy and population grow. Iran subsidizes the price of oil products heavily, to the tune of \$3 billion or so per year, resulting in a large amount of waste and inefficiency in oil consumption. The government also is forced to spend over \$2 billion per year to import oil products (mainly gasoline), which it cannot produce locally.

In April 2004, as part of an effort to curtail the rise in gasoline subsidy expenditures, gasoline consumption and imports (both of which are growing rapidly), parliament voted to more than double gasoline prices, to around 95 cents per gallon. Currently, Iran's gasoline prices are amongst the cheapest in the world. In November 2003, the government announced that it might even be forced to start rationing gasoline.

State-owned National Iranian Oil Company (NIOC)'s onshore field development work is concentrated mainly on sustaining output levels from large, aging fields. Consequently, enhanced oil recovery (EOR) programs, including natural gas injection, are underway at a number of fields, including Marun, Karanj, and the presently inactive Parsi fields. EOR programs will require sizeable amounts of natural gas, infrastructure development, and financing. Overall, Iran's oil sector is considered old and inefficient, needing thorough

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revamping, advanced technology, and foreign investment.

Second Thoughts

The Iranian Constitution prohibits the granting of petroleum rights on a concessionary basis or direct equity stake. However, the 1987 Petroleum Law permits the establishment of contracts between the Oil Ministry, state companies and local and foreign nationals and legal entities. Buyback contracts, for instance, are arrangements in which the contractor funds all investments, receives remuneration from NIOC in the form of an allocated production share, then transfers operation of the field to NIOC after the contract is completed.

The first major project under the buyback investment scheme became operational in October 1998, when the offshore Sirri A oil field (operated by Total and Malaysia's Petronas) began production at 7,000 bbl/d (Sirri A currently is producing around 20,000 bbl/d). The neighboring Sirri E field began production in February 1999, with production at the two fields expected to reach 120,000 bbl/d.

In March 1999, France's Elf Aquitaine and Italy's Eni/Agip were awarded a \$1 billion contract for a secondary recovery program at the offshore, 1.5-billion-barrel Dorud oil and natural gas field located near Kharg Island. The program is intended to boost production from around 136,000 bbl/d to as high as 205,000 bbl/d. Eni is also involved, with a 38.25 percent stake. The field, which contains some 80 million barrels of reserves, started producing at a 20,000-bbl/d rate in early 2003, and reportedly reached 40,000 bbl/d in February 2004.

In May 2002, Iran's Oil



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4.5 percent; for 2004 it is expected to grow at slightly slower, but still healthy, 4.4 percent rate.

Iran's 127-billion-dollar budget for 2004-2005 reportedly was based on a price assumption for Iranian oil of around \$19.90 per barrel. This compares to an average price for Iranian crude oil in 2003 of around \$26 per barrel, and a forecast price for 2004 of around \$30 per barrel. Budget deficits in Iran have been a chronic problem, in part due to large-scale state subsidies -- totaling some \$4.7 billion per year -- including foodstuffs and especially gasoline. Higher oil export revenues in the past couple of years have helped ameliorate this situation, as Iran gains around \$900 million in revenues for every \$1 per barrel increase in the price of its oil.

Despite relatively high oil export revenues, the nation continues to face budgetary pressures, a rapidly growing, young population with limited job prospects and high levels of unemployment; heavy dependence on oil revenues; significant (but declining) external debt; high levels of poverty; expensive state subsidies.

Iran is attempting to diversify by investing some of its oil revenues in other areas, including petrochemicals. Iran also is hoping to attract billions of dollars worth of foreign investment to the country by creating a more favorable investment climate (i.e., reduced restrictions and duties on imports, creation of free-trade zones). In May 2002, the State Expediency Council approved the Law on the

During the first six months of 2004, Iran produced 4.1 million bbl/d of oil (of which 3.9 million bbl/d was crude oil), up from 3.9 million bbl/d in 2003. Iran's current sustainable crude oil production capacity is estimated at around 3.9 million bbl/d, which is around 0.1 million bbl/d above Iran's latest (August 1, 2004) OPEC production quota of 3.817 million bbl/d. Some analysts believe that Iran's capacity is lower, and that it could fall even further until new oilfield developments (Azadegan, Bangestan) come on stream in a few years. Iran's existing oilfields have a natural decline rate estimated at 200,000-250,000 bbl/d annually and are in need of upgrading and modernization.

With sufficient investment, it is widely believed

these problems, Iran has ambitious plans to double national oil production -- to more than 5 million bbl/d by 2009 and 7 million bbl/d by 2024. The country is counting on billions of dollars in foreign investment to accomplish this, but it is unlikely to be achieved without a significant change in policy to attract such investment. To date, the Economist Intelligence Unit (EIU) estimates that the country has attracted some \$15-\$20 billion in foreign investment for its hydrocarbons sector (the largest being Eni's investment in the South Pars gas field).

Iran exports around 2.6 million bbl/d, with major customers including Japan, China, South Korea, Taiwan, and Europe. Iran's main export blends include Iranian Light (34.6° API,



Iran is the largest heavy crude exporter in the Middle East.

Review Hindering Growth

By Samaneh Ekvam

Minister of Industries and Mines Eshaq Jahangiri recently said policies had been chalked out for the domestic auto industry. However, till date the ministry has not provided any details in this regard. Interestingly, various auto sector experts seem not to know about this development yet. Furthermore, it looks like parliament has not been informed either.

The question that arises is why have the policies related to the auto industry, one of the main industrial sectors monopolized by the government, not been made public?

One is bound to draw the conclusion that since the MPs are opposed to foreign cooperation in the local auto industry and as the backbone of the new policies is cooperation with foreign parties, the Ministry of Industries and Mines wants to pursue the matter in a covert manner!

Some people think that as long as we have an expert workforce for manufacturing various automotive parts, it is improper to continue to assemble low quality foreign cars.

In the meantime, most lawmakers maintain that the government should not waste the country's assets by investing huge amounts of money in joint ventures with foreign auto companies. The Ministry of Industries and Mines should immediately notify the Majlis of the issue of foreign cooperation in the auto industry and clarify why Iran is not involved in the design phase despite the abundance of university graduates and professors in related fields as well as industrial experts.

The government has invested large sums of money for nurturing these experts and it is disgraceful that a plan for mere assembly of auto parts is to be implemented. In the era of technology, there is need to become more involved in design and building and mere involvement in the assembly phase does not suffice. Above all there is an urgency to reinforce the indigenous production sector so that it can progress according to international standards.

Such joint ventures with foreign firms will kill the creativity and initiative of local experts. It is crucial that the Ministry of Industry and Mines reviews its policies to protect national interests. The government needs to support the local auto industry so that it finds a share in the international market, instead of adopting covert strategies that could hinder national industrial growth.

Ministry signed a \$585 million buyback contract with NIOC subsidiary PetroIran to develop the Foroozan and Esfandiar offshore oilfields. PetroIran is expected to increase production at the fields from around 40,000 bbl/d at present to 105,000 bbl/d by late 2005.

Recently, Iran appears to have had some second thoughts about buybacks (including charges of corruption, insufficient benefits, and also worries that buybacks are attracting too little investment), and reportedly is considering substantial changes in the system. In late May 2002, Canada's Sheer Energy became the first foreign company since Eni's Darkhovin deal to reach agreement (\$80 million to develop the Masjed-e Suleyman, or MIS, field) under the Eni terms.

In January 2004, Iran announced modifications to the buy-back model, extending the length of such contracts from the current 5-7 years to as many as 25 years, while allowing for continued involvement of oil companies after the field is handed over to NIOC. In a bid to maintain its role as a major energy supplier in the world, Iran says it welcomes foreign investments to further develop its oil and gas fields through employment of advanced technology. Without foreign assistance, the oil-rich country would not be able to keep up with world demand, and may lose its advantage as a key oil supplier; something the economy cannot afford.