Iraqi Oil…
The Morning After

CSIS Energy Chairman Robert Ebel participated in the State Department project, the Future of Iraq, as a member of the working group focused on oil. A recent *New York Times* (10/19/03) article argued that the work from this project predicted many of the post-conflict challenges. This presentation provides a general overview of several main conclusions of the Oil Working Group. This presentation was first given and posted in January 2003. It was updated in March to reflect further working group meetings.

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The Morning After

Robert Ebel, CSIS Energy Program

There are 3 "Givens" When *The Morning After* Arrives…At Least in the Eyes of the Iraqi Opposition

1. There will be no occupational army
2. We Iraqis will govern
3. The oil sector is ours, to develop as we envisage

   Our first task will be to restore law and order and to supply food and fuel to the population

To Better Understand the Iraqi Oil Future, First Look at the Past

- Proven oil reserves of 112 billion barrels, second only to Saudi Arabia but considerably understated
- Oil sector nationalized in 1972
- Peak production of 3.5 million b/d reached in 1979

To Better Understand the Iraqi Oil Future, First Look at the Past

- Never attained again, as wars and then sanctions have interfered
- Had recovered to about 2.8 million b/d in 1989, but Gulf War depressed output to less than 0.3 million b/d in 1990
- Next recovery came with institution of "Oil for Food" program

To Better Understand the Iraqi Oil Future, First Look at the Past

UN "Oil for Food" Program

- Started in December 1996
- Oil sold in return for goods not denied by UN Sanctions
- Volume of oil sold by Iraq not mandated; Can sell as much or as little as it wishes

Oil for Food Program

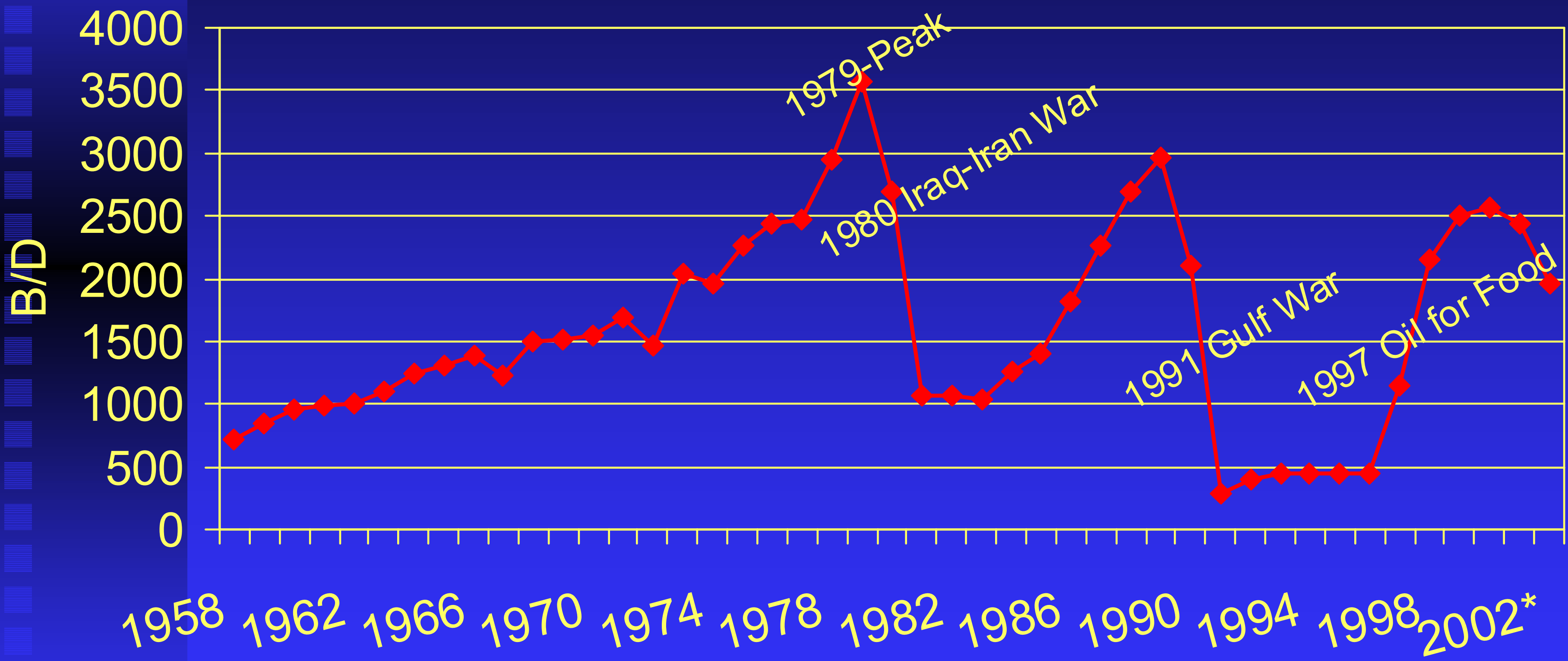
Where Does the Money Go?

Key Allocations, December 2002 – June 2003

Category	Percent of total
Food	29.0
Food handling	5.7
Oil	12.2
Agriculture	9.0
Electricity	5.5

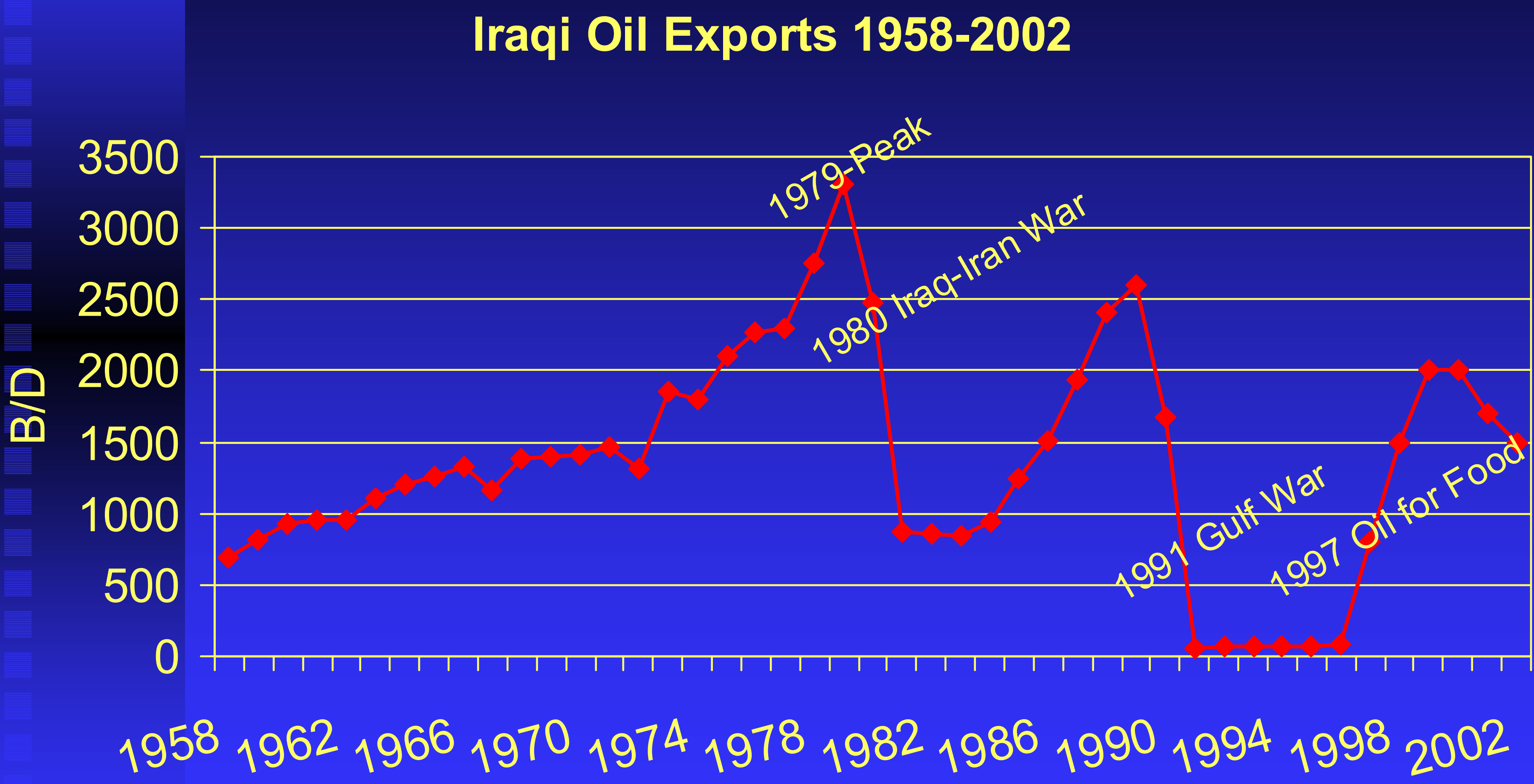
And 22 additional categories

Iraqi Oil Production 1958-2002



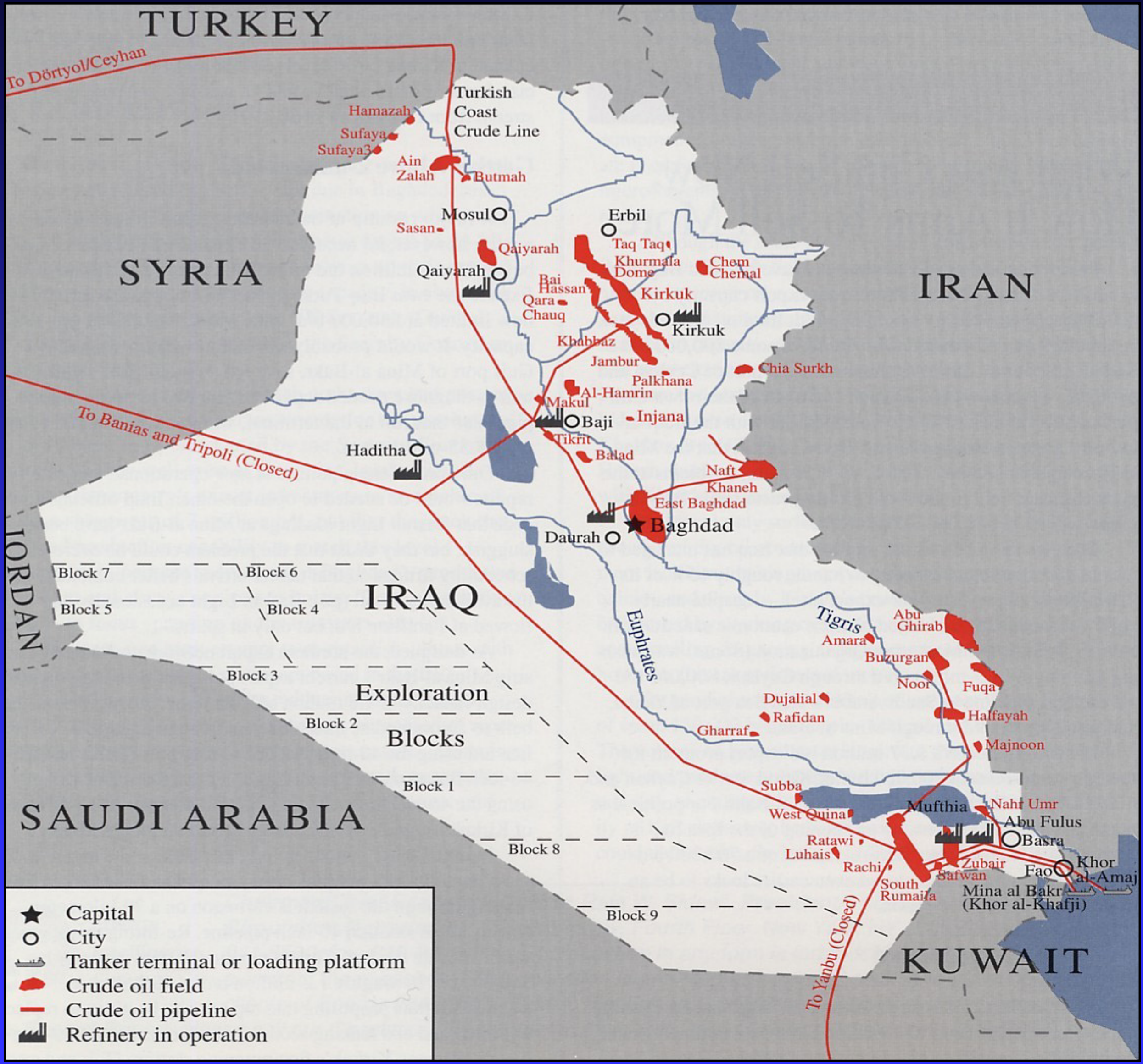
* 2002 figure is the 10 month average

Iraqi Oil Exports Have Closely Tracked Production



* 2002 figure is the 7 month average

Iraqi Oil Today



Energy Intelligence Group, 1998

Iraqi Oil Today

- Production capacity: around 2.6-2.8 million b/d
- Declining by 100,000 b/d annually
- Domestic consumption: some 400,000 b/d
- Volumes smuggled: also 400,000 b/d
- “Oil for Food”: 2 million b/d

How Might the Opposition View the Iraqi Oil Future?

- In theory could replace Saudi Arabia, the only country able to do so
- Can export avoiding the Gulf and Straits of Hormuz, thus providing additional security of supply
- Could be the deciding factor in world oil supply and demand
- Looking initially to regain past share—13.1% of OPEC production

Challenges to the Oil Sector

- Many experienced engineers and geologists have left. Will they return?
- Drilling and workover rigs and crews to manage them (biggest challenge of all), the latest oilfield technology, know-how, and managerial skills are all badly needed

Other Constraints

- Oil revenues needed to pay for imports and for reconstruction of the economy
- But war reparation payments, to Iran and Kuwait, must be cancelled. Viewed as a burden on the people
- Not enthusiastic about privatization. Could perhaps privatize downstream, but not upstream
- Concessions are out of the question; Term is unacceptable; Need a substitute.

Oil Field Problems

- Over-production at Rumaila and other fields
- Water encroachment
- High production decline rates
- Pipelines in poor shape
- Refineries need major upgrading; Current capacity around 400,000 b/d

The Saybolt Findings

- Saybolt International, a Dutch firm, visited Iraq on two occasions—March 1998 and January 2000—at request of UN, to evaluate the health of the Iraqi oil sector
- Their findings underscored the sector's "lamentable" state

The Saybolt Findings

- Observations from the report on the January 2000 visit:

The group has to report that the previously noted lamentable state of the Iraqi oil industry has not improved. It is apparent that the decline in the condition of all sectors … continues, and is accelerating in some cases. This trend will continue, and the ability… to sustain the current reduced production levels will be seriously compromised, until effective action is take to reverse the situation.

The Saybolt Findings

- But were these findings wholly impartial? Probably not.
- Both visits made the case for accelerated delivery of spare parts and equipment, contracts for which were being held up by the United States

Which is More Important?

- Oil field data

  or

- Oil sector infrastructure

Consensus held that **infrastructure** was more important.

- Data are available outside the country
- It is thought that just 7 fields provide the bulk of total Iraqi oil production.
  - Kirkuk in the north—700,000 b/d
  - Rumaila in the south—1.25 million b/d
- Could Coalition Forces immediately seize these fields, to protect operating personnel, data, and infrastructure?

Historic Precedence

According to International Laws Governing Warfare:

- Coalition forces have the right to produce Iraq's existing oil wells
- To use the proceeds to pay costs of occupation
- But military is prevented from takeover of private property

US government on record that drilling new wells in occupied territory is unlawful

Source: Oil and Gas Journal, 4 Feb 03

Contract Status

- First: Review all exploration and production contracts
- Certain of the opposition proposed canceling all contracts
- 2 key contracts have been signed: with Russia (Lukoil; cancelled again) and with China (CNPC)

Iraqi Financial Obligations Almost Insurmountable

- Gulf War Compensation $199 billion
- Foreign Debt $127 billion
- Pending Contracts $57.2 billion*

  *Primarily oil and telecommunications

- Future oil revenue far too small to accommodate every need

Iraq Will Negotiate From a Position of Strength

- Huge proven reserves
- Low production costs
- High quality crudes
- Easy access to ports of export

The Morning After, What To Do?

- First step: Assess the health of the oil sector
- Scope of effort defined by which scenario is realized
- What will it take, in $$$ and in time, to restore to prewar levels?
- Assemble groups of experts, Iraqi and non-Iraqi, to conduct the assessments
- But, who will pay?

Iraq’s Original Long Term Goals

- Forecasts issued in 1995:
  - First stage: 4.2 million b/d
  - Second stage: 5 million b/d by 2000
  - Third stage: 6 million b/d by 2010

What Might Future Production Levels Look Like?

- Takes time—between 5 to 7 years—to translate reserves into production
- 3.2 to 3.5 million b/d can be reached in the short term
- Some projected 5.5 to 6 million b/d in 8 years (i.e., by 2010)
- Others thought 4.2 million b/d by 2010

My Take?

- Key will be which scenario plays out
- If oil fields not damaged, could hit 4 million b/d by 2010
- If needed investment is forthcoming
- But no policy of flooding the oil market, as some think
- Impact and influence of Iraqi opposition *the morning after?*