22/01/1999

`Petronas has major decisions to make in oil industry's new era'

Jennifer Jacobs; Pratap Parameswaran

PETROLIAM Nasional Bhd (Petronas) has some strategic and tactical decisions to make in the emerging new era of the oil and gas industry in which global pressures have forced its competitors into mega mergers.

Bain & Co (Asia) Inc managing director Mark Daniell said Petronas has some major choices ahead of it based on short- and long-term pressures on the industry.

He pointed out that oil is on a price experiential curve whereby for each billion barrels of oil pulled out of the ground, the last barrel is significantly less expensive than the first, meaning a systematic long-term decline in prices.

In addition, he said, along that systematic long-term decline, there are fluctuations in oil prices based on short-term supply and demand such as the present crude oil price which has dipped below the US$10 (US$1 = RM3.80) a barrel and is unlikely to recover in the near future.

According to Ratings Agency Malaysia's Economics Chartbook 1997/1998, the failure of members of the Organisation of Petroleum Exporting Countries (Opec), which collectively account for 40 per cent of world oil output, to agree on cuts in production quotas is singled out as one of the key reasons for the price drop.

Daniell said that in the short term, Petronas has to decide if it wants to draw down on its reserves at a time when it does not get much renumeration for its assets, or leave it in the ground and buy cheap oil in the marketplace through its trading company, until oil prices recover.

However, he pointed out that analysts will be waiting to see, not only the group's short-term tactical issues of production, refining, trading and retail pricing, but also the long-term strategic moves which will chart its course in a future characterised by systematically lower oil and gas prices.

While its global competitors such as Exxon, Mobil, BP and Amoco are being forced into mega-mergers because of declining oil prices, he said, in Petronas' case, global competitive pressures need to be counterbalanced with the unique role Petronas plays in the Malaysian economy.

Daniell was asked to comment on Prime Minister Datuk Seri Dr Mahathir Mohamad's statement on Tuesday that the country can reduce or even stop oil production if prices drop too low.

Earlier this week, Kuwait warned that oil prices could fall to US$5 a barrel this year unless Opec members take urgent measures.

Brent crude, the North Sea benchmark, is trading at about US$10.60 a barrel.

Analysts contacted said many oil-based companies listed on the Kuala Lumpur Stock Exchange will not be affected much by the drop in prices.

"Petronas Gas Bhd will not be affected as it is only involved in transmission and as such not directly involved," one analyst said, adding that it has a profit agreement contract with its one customer - parent company Petronas.

The other Petronas subsidiary, Petronas Dagangan, will see its margins expand with lower oil prices as it operates an automated pricing mechanism which has a two-month lag.

"So if oil prices weaken they will stand to benefit," he said.

Shell Bhd will also not be affected greatly as it only has a small refining operation and is involved mainly in sales and marketing, another

analyst said.
However, he asked whether independent power producers (IPPs), who are now paying less for fuel, will now lower their prices. "The IPPs use natural gas, the price of which is fixed to the price of fuel," the analyst said.

(END)