

## **Canadian mess should be Petronas' wake-up call**

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**Petronas' messy RM100 billion Canadian LNG (liquefied natural gas) project is a perfect example of the company's hubris when investing overseas. Will it be a wake up call and force Petronas to change its free-spending ways?**

A project that began in 2012 with the US\$5 billion (RM18 billion) purchase of Canadian oil and gas company Progress Energy Resources is now a potential US\$30 billion (RM109 billion) albatross around Petronas' neck.

The Canadian investment (one of the biggest in Petronas' 41-year history) was hailed in 2012 as a project that would rejuvenate Petronas and catapult it to the upper echelons of major oil and gas players. Now, the project is hanging by a thread.

Petronas' Progress Energy acquisition was closely linked with the Pacific NorthWest LNG project in British Columbia, which is now in limbo.

Petronas has a 62% stake in Pacific NorthWest and it includes plans for an LNG terminal which will enable Petronas to sell and transport Progress Energy's shale gas assets from British Columbia to lucrative Asian markets. Without the all-important export terminal, Petronas' Progress Energy purchase diminishes in value. Overall, the project is estimated to cost Petronas US\$30 billion over 25 years.

Although Wan Zulkiflee Wan Ariffin, Petronas' new president and group CEO, assures that the Pacific NorthWest project's FID (final investment decision) will be decided soon after numerous delays, an air of uncertainty still hangs over the troubled project.

On May 13, a community of Canadian aboriginals rejected Petronas' compensation offer of C\$1 billion (RM2.9 billion) to construct the LNG terminal on their land in Lelu Island. Petronas says that the project will still go ahead, regardless of the aboriginals' consent, while the natives themselves are claiming otherwise.

The prevailing mood about the massive Pacific NorthWest LNG project is now decidedly more nervy and less triumphant than it was a few years ago. What has gone wrong?

Obviously, the plunge of crude oil prices in the last 12 months threw a spanner in the works. What looked like possibly a sure bet just three years ago now looks like it could become a major financial burden for Petronas.

Petronas' profits have fallen for the second consecutive quarter, unheard of in its history. Petronas has been forced to slash their operating expenditure (opex) and capital expenditure (capex) by the tens of billions of dollars.

Volatile LNG prices may make the Canadian project (and perhaps many other overseas) increasingly unviable. Question marks over the disputed export terminal in Lelu Island, a crucial component of the British Columbia project if it is to realise its full commercial potential, may jeopardise Petronas' future in this project.

But Petronas only has itself to blame for its Canadian predicament.

For so long, Petronas has not been fully transparent in its overseas investments. Incredulously, for such a large organisation with huge public interest, Petronas does not reveal whether it makes money or not in each its foreign ventures.

It only gives breakdowns according to business segments and geographical revenue, but not on a case-to-case basis.

For example, can the public find out exactly how much money Petronas has made or lost in its troubled project in Sudan? There is no such disclosure in Petronas' financial accounts.

Despite Petronas' meteoric rise in the oil and gas corporate landscape in just over 40 years, its lack of full financial disclosure is a major chink in its armour.

Its disclosure standards have been found wanting. Petronas has done little to address this weakness despite harbouring lofty ambitions to reach the same standards of other oil majors such as Shell and ExxonMobil.

Each splurge overseas is usually accompanied with the usual ballyhoo, without any need to justify the risks and rewards. Sinking billions of dollars into a foreign project is seen as an unquestionable necessity for Petronas' survival, to replenish the country's dwindling energy reserves, without considering any possible alternatives.

Are there any checks and balances to prevent Petronas' top executives from throwing good money after bad?

Hardly. There is little incentive or pressure to reform its foreign spending because profits or losses in each high-risk overseas venture are not revealed in the company's accounts. The impetus is just to throw the dice on a high stake bet and move on to the next if one fails.

In the days of US\$100 oil, this was probably the norm for high-flying Petronas. Now that things have changed dramatically with the crash of oil prices, Petronas will definitely have to be more circumspect.

Which brings us back to Petronas' RM100 billion Canadian misadventure. Clearly, it may have bitten off more than it could chew.

Did Petronas foresee that it could be held to ransom by the aboriginals? Did its due diligence for this project reveal such resistance and were these factors taken into account financially? How much exactly is Petronas willing to pay compensation to the aboriginals and how would this impact Petronas' profits for this venture?

In retrospect, it would seem now that Petronas was quite reckless in its US\$5 billion purchase of Progress Energy in 2012 when the Pacific NorthWest project, one that is integral to the whole thing being commercially viable, is still not approved three years later.

Even if it is eventually approved, will it all have been worth Petronas' troubles?

This brings us back to other argument about Petronas' foreign ventures. Should it step beyond Malaysian shores at all?

Under the Petroleum Development Act 1974, the state oil company's most important role is as the guardian of the country's petroleum resources, not to become an international oil major.

Nothing in the Act mandates Petronas to risk public monies overseas unnecessarily, no matter how admirable its entrepreneurial ambitions may be.

Foreign oil and gas ventures, especially in upstream exploration and production, require massive capital outlays.

Although its returns are potentially huge as well, other external factors beyond Petronas' control such as price volatility and geopolitics also come into play.

Although it may boost top line numbers and give Petronas greater global visibility and stature, the overall returns on Petronas' investments overseas could be marginal at best, due to excessive entry costs.

It could also be the case that Petronas' domestic profits are subsidising its risky ventures overseas.

The plunge of oil prices makes a strong case for Petronas to focus on its domestic businesses and reduce its risky foreign exposure.

Indeed, its ill-advised Canadian venture should be a big wake-up call for Petronas to mend its free-spending ways.

The nation cannot afford Petronas to indulge in another messy foreign outing such as the RM100 billion Canadian LNG project, unless the company can fully disclose each individual project's profits and losses to public scrutiny and for Petronas to be accountable for any missteps.

Until then, maybe Petronas should just pack up and bring it all back home.

**GRRRRR!!!**

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