

Insights and Commentary from Dentons

The combination of Dentons and Adepetun Caxton-Martins Agbor & Segun offers our clients access to 12000+ lawyers in 203 locations and 80 countries around the world.

This document was authored by representatives of Adepetun Caxton-Martins Agbor & Segun prior to our combination's launch and continues to be offered to provide clients with the information they need to do business in an increasingly complex, interconnected and competitive marketplace.

COVID-19 : IMPACT ON THE NIGERIAN OIL AND GAS INDUSTRY

APRIL 2020

Obsolete legal, fiscal and regulatory frameworks, uncertainty over pending laws, insecurity and bureaucratic inefficiency have all been identified as perennial challenges facing the Nigerian oil and gas industry (“the Industry”). The outbreak of the novel coronavirus (COVID-19) and subsequent measures implemented to flatten the curve have resulted in disruptions of epic proportions – the Industry is not exempt from these disruptions and this poses a new challenge for the Industry.

COVID-19 AND THE GLOBAL OIL MARKET

It is no longer news that the spread and impact of COVID-19 is now global, with countries, economies, businesses, sectors and industries all heavily impacted. The global oil market is not spared. Worldwide, the oil industry has already taken serious hits as major economies are on lockdown, which has significantly reduced the demand for crude oil. Generally, factories, plants, refineries and businesses have shut down or scaled-down their operations due to necessary measures implemented to break the COVID-19 transmission chain.

The global oil market recently posted its worst quarterly performance ever, dragged down by COVID-19 and an unwelcome global price war. According to published reports, US traded oil West Texas Intermediate (WTI) crude is down as much as 66%, while Brent crude shed as much as 65% in the same time period. WTI trades at roughly US\$20.40 *per* barrel, while Brent crude is about US\$22.71 *per* barrel¹.

The unprecedented plunge in crude oil prices is poised to change the global oil market with fewer companies being able to withstand the impact of low prices. Some of the grim pictures painted by commentators are that up to 20% of the offshore workforce will be out of job², companies will scale-down projects by up to US\$131 billion and delay projects³, and more than 200 of Europe’s mid and small sized oilfield service companies are set to become insolvent⁴. In fact, the world’s biggest oil and gas companies are already slashing capital spending this year following a collapse in oil prices. Cuts announced by nine major oil

¹ <https://markets.businessinsider.com/commodities/news/oil-price-plunges-worst-quarterly-performance-ever-coronavirus-war-most-2020-3-1029051076>; <https://www.oil-price.net/>.

² <https://www.offshore-technology.com/features/coronavirus-covid-19-offshore-cost-opec/>

³ <https://www.oilandgasmiddleeast.com/drilling-production/36438-covid-19-and-oil-price-war-could-slash-two-thirds-of-2020-oil-and-gas-project-sanctioning>

⁴ <https://energy.economictimes.indiatimes.com/news/oil-and-gas/200-oilfield-service-firms-could-go-bankrupt-as-covid-19-slashes-5-bn-off-the-market/74713008>

companies, including Saudi Aramco, Exxon Mobil and Royal Dutch Shell, come to a combined US\$38 billion, or a drop of 22% from their initial spending plans of US\$175 billion⁵.



Furthermore, the market signals depict that not only will the demand for crude oil be low, but the global oil industry will experience insufficiency in crude oil storage facilities. Less demand for oil globally, has resulted in storage facilities, refineries, terminals, ships and pipelines reaching their full capacity⁶. Demand is falling so fast relative to supply that the main concern of many producers will shift to finding an outlet for their crude oil. Indeed, it is speculated that crude oil prices could turn negative⁷.

IMPACT ON THE NIGERIAN OIL AND GAS INDUSTRY

Decreased level of demand for crude oil - Without doubt, the decline in oil demand and the low crude price caused by COVID 19 and the global price war will adversely impact a crude oil-based economy like Nigeria. The outbreak of COVID-19 in many of the countries that purchase crude oil from Nigeria and the measures implemented have affected Nigeria's market share. Major buyers of Nigeria's crude oil, such as India, Spain, France, Italy, Canada, have been impacted by COVID-19, which has taken a negative toll on their economies and decreased their level of demand for crude oil. The obvious effect of the decline in crude oil demand is that there is a supply glut - excess supply of crude oil in the market with few or no buyers.

Buyer scarcity - According to the Group Managing Director of the Nigerian National Petroleum Corporation ("NNPC")⁸, Mele Kolo Kyari, Nigeria has had difficulties in finding buyers for its crude oil and liquified natural gas (LNG) cargoes. NNPC recorded that about 50 cargoes of crude oil and 12 cargoes of LNG were stranded on the international market as at 11

⁵ <https://www.reuters.com/article/us-global-oil-majors-capex-graphic/oil-majors-slash-2020-spending-by-20-after-prices-slump-idUSKBN21J516>

⁶ <https://edition.cnn.com/2020/04/01/business/oil-prices-crash-storage-space/index.html>

⁷ <https://www.cnn.com/2020/04/01/coronavirus-oil-prices-could-turn-negative-as-storage-nears-capacity.html>

⁸ The NNPC is the national oil company through which the Federal Government of Nigeria regulates and participates in the country's oil and gas industry

March 2020. As a result of its inability to dispose of these cargoes, NNPC discounted the official selling prices for Bonny Light and Qua Iboe by US\$5 per barrel to clear a glut of unsold April-loading cargoes⁹.

Increased pressure on the Naira and foreign reserves - The continuous drop in the price of crude oil in the international market has already taken a toll on the nation's crude revenue dependent economy - oil and gas account for over 90% of Nigeria's foreign exchange earnings and more than 60% of the country's earnings¹⁰. According to the Minister of Finance, Budget and National Planning, Zainab Ahmed (the "Minister of Finance"), COVID-19 has put "*increasing pressure on the Naira and foreign reserves as the crude oil sales receipts decline and the country's macro-economic outlook worsens*"¹¹. Nigeria's budget for 2020, which was set at an oil benchmark of US\$57 per barrel, has now been reviewed against the background of the impact of the Coronavirus pandemic on the global economy and global oil prices. Following the review of the 2020 budget, the Minister of Finance confirmed a review of the budget oil benchmark from US\$57 to US\$30 per barrel¹².

DPR declaration of force majeure - The Department of Petroleum Resources (the "DPR" – the regulator of the Industry) in response to measures introduced by the Nigerian government, recently directed oil operators, contractors and service providers to limit the number of personnel at project and construction sites and declared the current situation should be considered as "*force majeure*"¹³. No doubt these measures will impact production in Nigeria

Cost cutting measures - Oil companies in Nigeria, like their counterparts in other parts of the world, are likely to embark on cost cutting measures, including scaling down on projects and reducing their workforce. A major Nigerian independent oil and gas firm, Seplat Petroleum Development Company Plc, is already looking to cut costs by at least 30% to counter a crash in crude prices¹⁴.

Premium motor spirit price review - It is not only the upstream sector of the Industry that is affected – the downstream sector is also impacted. In reacting to the plunge in crude oil prices, the Petroleum Products Pricing Regulatory Agency¹⁵ recently reviewed the pump price of premium motor spirit downward from N145 to N125 *per* litre effective 19 March 2020. A further reduction to N123 *per* litre was made effective 1 April 2020. The new price, which will last throughout the month of April, was introduced on the back of the *continuous decline* in the price of crude oil in the international market¹⁶.

⁹ <https://punchng.com/nigeria-slashes-crude-selling-prices-to-woo-buyers/>

¹⁰ <https://www.pulse.ng/news/local/impact-of-coronavirus-on-nigerias-oil-and-gas-sector/fkx103r>

¹¹ <https://economicconfidential.com/2020/03/nigeria-economy-fragile-covid19-pandemic/>

¹² <https://punchng.com/fg-reduces-n252bn-privatisation-target-n1-5tn-customs-revenue/>

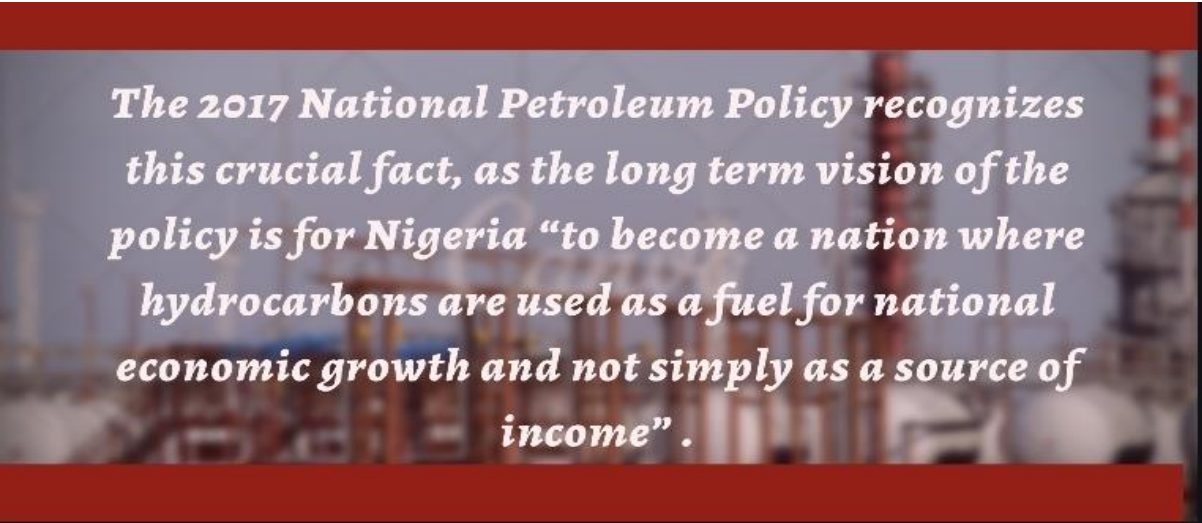
¹³ <https://www.dpr.gov.ng/reduce-workforce-at-project-sites-dpr-tells-operators/>

¹⁴ <https://punchng.com/nigeria-slashes-crude-selling-prices-to-woo-buyers/>

¹⁵ The Petroleum Products Pricing Regulatory Agency is an agency of the Federal Government of Nigeria responsible for monitoring and regulating the supply and distribution, and determining the prices, of petroleum products in Nigeria

¹⁶ <https://www.vanguardngr.com/2020/04/oil-price-slump-fg-further-slashes-fuel-price-to-n123-50-per-litre-2/>;
<https://www.pulse.ng/bi/strategy/nigerian-government-announce-a-reduction-in-fuel-price-effective-april-1/yc28bns>

WHAT NEXT?



The 2017 National Petroleum Policy recognizes this crucial fact, as the long term vision of the policy is for Nigeria “to become a nation where hydrocarbons are used as a fuel for national economic growth and not simply as a source of income” .

Diversification, Diversification, Diversification - There is no doubt that Nigeria needs to diversify its economy from its current reliance on crude oil revenues. The 2017 National Petroleum Policy recognizes this crucial fact, as the long-term vision of the policy is for Nigeria “to become a nation where hydrocarbons are used as a fuel for national economic growth and not simply as a source of income”. The COVID-19 pandemic is a cruel reminder that the time to act is now, and the Federal Government of Nigeria (the “Federal Government”) must broaden its horizon and increase its investments in the non-oil sectors such as agricultural, real estate, financial technology, manufacturing *etc.* The diversification of the Nigerian economy is key and is a medium to long term plan.

Interim government measures - The short-term outlook for the Nigerian economy and the Industry will ultimately depend on how quickly governments move to contain COVID-19 and how quickly the recent global oil price war is contained. However, in the interim, the Federal Government must roll out measures to protect oil and gas operators, contractors, service providers and their workforce.

CBN Stimulus Package - In this regard, the stimulus package by the Central Bank of Nigeria (“CBN”) is commendable. The CBN introduced the N50 billion Targeted Credit Facility (“TCF”) as a stimulus package¹⁷, which seeks to support households and micro, small and medium enterprises (“MSMEs”) affected by the COVID-19 pandemic. While the activities within the Industry are not covered under the CBN TCF, it seeks to cushion the adverse effects of COVID-19 on MSMEs’ operating in agricultural, hospitality, health, manufacturing, airline and trading sectors; it also provides credit to MSMEs to expand their productive capacity through equipment upgrade, and research and development.

Restructuring – Specifically in relation to key sectors including the Industry, the CBN granted leave to all deposit money banks to consider temporary and time-limited restructuring of the

¹⁷ <https://www.cbn.gov.ng/Out/2020/FPRD/N50%20Billion%20Combined.pdf>

tenor and loan terms for businesses impacted by the COVID-19 pandemic - this is a step in the right direction¹⁸.

Emergency Economic Stimulus - The House of Representatives introduced the Emergency Economic Stimulus Bill 2020 “*to provide for relief on Corporate Tax Liability, suspension of import duty on selected goods and deferral of residential mortgage obligations to the Federal Mortgage Bank of Nigeria for a fixed term to protect jobs and alleviate the financial burden on citizens in response to the Economic Downturn occasioned by the outbreak of COVID-19 disease and for related matter*” – the Bill. It is important that the Bill is fast-tracked through the legislative process because of its obvious benefits. The Bill provides for fiscal relief for taxpayers in key sectors of the economy by incentivizing employers to retain staff during the economic downturn as well as eliminating fiscal bottlenecks on the importation of medical and personal protection equipment to combat COVID-19. Particularly, the incentives for employers to retain staff will effectively protect the employment status of Nigerians who may otherwise become unemployed as a consequence of the prevailing economic realities caused by COVID-19. The Bill also provides for a moratorium period of 6 months on mortgage obligations for individuals.

However, a point to note is that the employee retention incentive provided under the Bill will not apply to employers partly or wholly under the Petroleum Profit Tax Act Cap P13 LFN 2004 – these would be upstream companies operating in the Industry. This raises a query – what is the basis for the exclusion: the stimulus measures captured in the Bill should also be extended to companies operating in the entire value chain of the Industry.

CONCLUSION

There is no gainsaying the fact that the impact of the COVID-19 pandemic will be far reaching and will remain within the Industry well after some normalcy returns to the daily life of people and companies. However, a well-thought out stimulus package, which is not selective in application, could ensure that the Industry is able to bounce back much quicker than expected. As already highlighted, the continued pressure on oil prices is leading to oil companies cutting back on their investments and workforce; and to avoid a total shutdown in the economy resulting from the downturn in the oil industry, the Nigerian government essentially, must lead economic diversification, effectively.

This article was written by Omolola Coker and Adebimpe Mosanya.

Omolola is a Senior Associate, Energy and Project Finance Group of Adepetun Caxton-Martins Agbor & Segun (ACAS-Law). Adebimpe Mosanya is a Trainee Associate, ACAS-Law.

¹⁸ CBN Circular to Deposit Money Banks and the General Public On: CBN POLICY MEASURES IN RESPONSE TO COVID-19 OUTBREAK AND SPILLOVERS March 16, 2020

ACAS-Law is a full service, corporate commercial law firm located in Lagos, Abuja and Port Harcourt, Nigeria, West Africa.

Further enquiries should be addressed to ocoker@acas-law.com.