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Brazil oilfield reveals local sourcing problem

By Joe Leahy

The Peregrino field operated in the Atlantic Ocean near Rio de Janeiro by Statoil is a throwback to the past when it comes to its local content requirements

The Peregrino field operated in the Atlantic Ocean near Rio de Janeiro by **Statoil**, Norway's state-run oil company, is a state-of-the-art operation.

The field's platform, the latest model of a "floating, production, storage and offloading" unit capable of processing oil and storing it, was built in China and Singapore last year. It is the most expensive yet commissioned by contractor Maersk FPSOs, with a price tag of more than $1bn.

But despite the Brazilian government's ambitious push to increase the local content of equipment used in its oil industry, Peregrino is a throwback to the past. The field's local content requirement is only about 35 per cent and consists mostly of wells and other underwater infrastructure. "In the beginning we looked to build [the floating platform] here but there was no capacity," says an engineer at Maersk FPSOs.

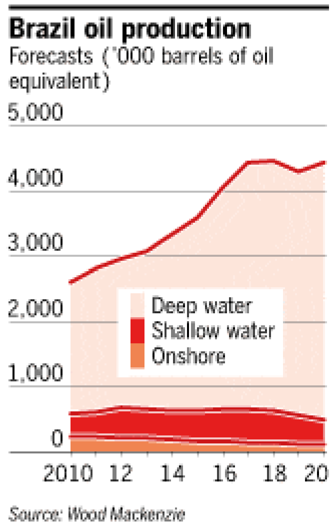
The project, which started to operate in April, illustrates the challenges facing Brazil as it tries to increase local content requirements for new production fields to 77 per cent.

Brazil's state-run operator Petrobras is investing $224bn between 2010 and 2014 to develop its huge "pre-salt" discoveries, lying below a two-kilometre deep salt layer under the seabed.

The vast potential of deepwater discoveries in Brazil is changing the profile of global oil companies, BG Group's doubling of its oil reserves being one example. The discoveries are also attracting numerous other multinationals specialising in research and development and oilfield services. Bain & Co this week announced the opening of its Rio office, which will specialise in oil and gas.

For most of the operators in Brazil, the chief hurdle will be how to negotiate increasing requirements for local content in a country that lacks the capacity to cope with the enormous demands of the coming decade. "Local content is going to be a huge issue," says Pedro Cordeiro, a partner at Bain.

The biggest strain is expected to be on Brazil's local shipbuilding industry. Petrobras alone is ordering a small navy of vessels. This month it placed an order for 21 drilling ships on top of seven already ordered. Last year Petrobras and its partners BG Group, Galp Energia and Repsol signed two contracts for the construction of hulls for eight floating platforms, or FPSOs, with Brazilian infrastructure firm Engevix Engenharia.



The challenge for Brazil is that its shipyards have not built FPSOs before. According to a report from consultancy Wood Mackenzie, Brazil will need 100 new oil platforms over the next decade, nearly half of them for Petrobras.

Of the 40 shipyards in Brazil, only four are believed to be capable of building FPSOs, the consultancy says. Some of the biggest names in shipbuilding, including South Korea's Samsung Heavy Industries and Singapore's Keppel, are participating. But it will take time for them to retool to undertake such a complex project as building a floating platform.

The need for more capacity has also led to a rush of proposals to build new shipyards in Brazil, with foreign investors such as Hyundai teaming up with Brazilian companies, such as OSX, controlled by the country's richest man, Eike Batista.

"Brazil could more than double its offshore facility construction capability, and crucially this capacity increase will include FPSO fabrication," says the Wood Mackenzie report.

But the question is whether capacity can be ramped up quickly enough and at reasonable cost. Petrobras is already coming under pressure from the government to curb costs amid signs it will need even more investment than expected to develop pre-salt.

Experts on local content say the challenge for the government is to “optimise” its local requirements. Flat targets for local content will reduce unemployment but not necessarily ensure the long-term success of the industry.

The best measure of whether the policy is succeeding will be the success rate of Brazilian shipyards and contractors in international open tenders, says Michael Warner, director of UK-based consultancy Local Content Solutions.

“Obligations to use less experienced local contractors may risk delaying the date at which a field produces oil or gas, potentially deferring hundreds of millions of dollars in revenues for both investors and for use by the host government,” he adds.

At Peregrino, engineers agree that Brazil and Petrobras have their work cut out in sourcing enough local content for pre-salt. Asked about Petrobras’ order for the eight FPSOs, one engineer says: “That is very courageous.”