DRILLING CONTRACTOR

DRILLING AHEAD

2001 spending plans promising; cash flow, gas prices are keys

John Kennedy, Contributing Editor

OIL PRICES HAVE PULLED back from the record levels set in 2000. And natural gas prices surely will, maybe to half the $9-10/Mcf level of recent months.

So will operators increase their E&D spending more in 2001 than they did last year?

Many say they plan to, some by large amounts. And it could very well happen.

Recent surveys of oil and gas company intentions vary, but the consensus appears to be that global E&P spending will be about 20% higher this year than in 2000.

And last year's spending, despite the common complaint that expenditures were lagging way behind the rise in oil and gas prices, was up worldwide by almost 15%.

That is according to the **Lehman Brothers** Original E&P Spending Survey, released in late December. At mid-2000, that survey concluded that worldwide spending would be up by 18.2%.

In North America, operators overspent their budget; elsewhere, they underspent, according to Lehman Brothers.

WHO WILL SPEND IN 2001?

Independents were particularly aggressive last year. A recent **Salomon Smith Barney** survey reports that independents spent 48% more in the US in 2000 than in the year before. Some are again planning increases, but some are cutting back, according to the Salomon survey.

Salomon reports that the 11 largest oil companies, led by **Royal Dutch/Shell** and **BP Amoco** plan to spend almost $41 billion in 2001, 14% more than last year. But **Total/Fina Elf** and **Texaco** do not plan increases, according to the survey.

The Lehman Brothers Original E&P Spending Survey concludes that the companies in the survey plan on 19.1% growth in worldwide E&P expenditures in 2001 compared with their estimated spending last year.

The Lehman Brothers survey also shows that in the US, independents have been the primary drivers of the recovery over the past 18 months and the group also plans the strongest gains in 2001.

The 231 independents in the Lehman Brothers group are budgeting an average of a 21.7% increase, according to the survey. Major oil companies are planning to spend about 15.9% more than they did last year on E&P activities. Together, operators will spend 19.1% more in 2001 in the US than last year.

In Canada, where recovery has been strong since the spring of 1999, the Lehman Brothers survey of 84 companies indicates they have budgeted an average 19.9% increase in E&P spending in 2001.

It's a bright picture by any measure.

SPENDING DRIVERS

Few expected the bottom-of-the-cycle oil and gas prices of early 1999 to last. Fewer still expected WTI and Henry Hub gas to climb to the thin-air altitudes they reached in late 2000.

Oil prices have come off their high and will likely move lower between the end of the northern hemisphere winter and the beginning of the driving season.

And natural gas prices will likely return to the $4-5/Mcf range soon.

Won't they?

At least, that is what operators seem to be expecting. Those responding to the Lehman Brothers survey based their spending plans on an average oil price expectation of about $25/bbl for WTI and $3.75/Mcf for natural gas.

In the survey, operators named cash flow is one of the two most important drivers of E&P spending. The top determinant was natural gas prices. Oil prices came in fourth, after prospect availability.

It's no surprise that operators—and consumers and regulators, for that matter—are watching natural gas. Three-fourths of

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CAPITAL WIRELINES

Proposed hours of service regs don't fit drilling contractor needs

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DOT HAULING REGULATIONS (Washington)—IADC recently filed comments to proposed changes in "hours of service" regulations by the **US Department of Transportation** Federal Motor Carrier Safety Administration which could have a severe adverse impact on oilfield rig moves. While intended to cover all commercial carriage, it would effectively eliminate a longstanding waiver for oilfield hauls. In the comment submitted by IADC Director-Land Operations **Joe Hurt**, IADC made the following points.

"The International Association of Drilling Contractors represents virtually the entire global drilling industry, including US land drilling contractors. Most of our members do not own trucks. But whether they own trucks or not, US land drilling contractors depend heavily on commercial motor carriers to move, rig up and supply their rigs.

"The **Interstate Commerce Commission** (ICC) issued the Oil Field Exception on 29 March, 1962 for good reason. Elimination of the Oil Field Exception that is currently part of 49 CFR §395 would seriously affect the ability of our members to provide energy for our nation.

"The number of additional drivers that would be required to move and rig up drilling rigs would increase by approximately 35%-45% for a large rig mover, and up to 100% for a small rig moving company. Currently, US land drilling contractors may have to wait 1-3 days or more for trucks to move a rig because there are not enough drivers or trucks.

"As stated in the current Oilfield Exemption (§395.1(d), 'the transportation of drilling rigs is highly technical and requires special equipment and specially trained drivers.' Nowhere in the revised regulation is this addressed.

"The proposed regulation would remove the flexibility needed by oilfield carriers to match the unique requirements of doing business in the oil and gas drilling industry."

"The process of disassembling a rig and reassembling it at a new location requires that drivers and their equipment spend time waiting to be loaded/unloaded. For safety reasons, rigging down and up is done during daylight hours and most states require that oversize/overweight loads move only during daylight. Changing the current regulation by removing the Oilfield Exception would greatly increase the cost of rig moves.

"§394.123(a) of the proposed regulation states: 'Your operations must fit within one of the categories described in §394.121, and you must adjust your hours of operation to conform to the requirements applicable to that type of operation.' This 'one size fits all' approach to the five types of operations for drivers does not fit oilfield rig movers.

"The oil and gas drilling industry operates around the clock. Support services associated with them, such as commercial motor carriers, are required to operate on the same basis. The proposed regulation would remove the flexibility needed by oilfield carriers to match the unique requirements of doing business in the oil and gas drilling industry.

"For these reasons, IADC recommends that these proposed regulations be withdrawn and any new proposed changes to the HOS regulation retain the Oilfield Exception in §395.1(d) and §395.1(g) Sleeper berths."

It remains to be seen whether the Bush Administration will withdraw the proposed rule changes, but the hauling industry is encouraged by widespread support in Congress for withdrawal or substantial modification. ■

active US rigs were drilling for gas last year and it is widely agreed that meeting US demand over the next decade will be an enormous challenge.

Other spending drivers (in, respectively, 5th, 6th, and 7th place in the survey) included drilling success, capital availability and drilling costs.

DRILLING COSTS

In this group of operators, at least, drilling costs do not seem to be of great concern. A word of caution, however: About two-thirds of the companies said higher rig rates could have an impact on their drilling programs.

Most operators expect drilling costs to rise this year. Most said they expect rig rates to increase and most expect costs to be higher "everywhere" in 2001.

But the operators participating in the survey are taking actions to mitigate the impact of higher costs.

"More companies are attempting to lock in suppliers (particularly rig companies) for long-term contracts or multiple well deals," said the report on the survey. "Absent this, they are putting more work out for bid and/or doing more turnkeys."

What technologies have the greatest impact on the E&P business? Survey responses rated 3D seismic #1, followed in order by horizontal drilling, fracturing/stimulation, directional drilling, bits, underbalanced drilling and deepwater technology.

A final concern of a large majority of the companies surveyed: The availability of equipment and people.

VOLATILITY REMAINS

It appears the E&D spending cycle may be catching up with the oil and gas price cycle. For several reasons—the most important of which is a precarious oil and gas supply/demand balance—it looks like a strong year for drilling.

But keep in mind that cycles—of oil prices, E&P spending, hiring, whatever—often overshoot the optimum level.

Both on the way up and on the way down.

Oil and gas will still be commodities in 2001. The price of a commodity in the short term is volatile; in the long term commodity prices tend to decline.

In the face of volatility and cost pressures, continued improvement in efficiency and safety—and technical and organizational innovation—are still the keys to success for drillers.

Even in a strong year. ■