



Activity, dayrate outlook remains mixed for US land drillers faced with softening prices, stacked rigs, more newbuilds

By Linda Hsieh, associate editor

A PERFECT STORM appears to be brewing above the US land drilling market, said Mr Wm Stacy Locke, president and CEO of Pioneer Drilling.

One, an overall warm winter left natural gas underground storage above the 5-year historical average. “A cold snap in February bailed us out somewhat, but we still ended winter above that 5-year average,” he said. For operators, that puts natural gas prices in question for this year.

“Two, there are stacked rigs in every market around the country — not many, but every market has some — which is putting downward pressure on dayrates. At the same time, because of newbuilds, the overall rig count continues to increase at a time when normally you’d expect it to go down. If the rig count continues to increase, US natural gas production may not fall off relative to prior-year production levels,” Mr Locke said. “It’s a very unusual situation going on in the industry.”



Pioneer Drilling's Rig 55 works in the Barnett Shale with Fort Worth in the background. The rig is a 1,500-hp electric rig built in 2005.

On the bright side, by April 2007, natural gas prices appeared to have firmed up, Mr Locke said, citing a spot price of \$7.50. "That's much better than anyone thought it would be in December. I don't think anybody expected gas prices to be quite this strong. They've turned out to be more resilient than we thought."

However, both natural gas prices and dayrates are likely to decline again in the next few months, he said. "The first weak quarter of the last several years was the 4th quarter of 2006. The first quarter of 2007 was the start of a slightly more severe decline, and I think it won't be the bottom quarter (of this year). I think dayrates will bottom out in the 3rd quarter, then we'll start to see improvements in the 4th quarter and into next year."

One major problem is the newbuilds ordered last year and being delivered this year. Pioneer added 6 new rigs in the fiscal year ending 31 March 2006 and 11 in the fiscal year ending 31 March 2007. The latest rig, contracted more than a year ago, was scheduled to be delivered from a north Houston yard in late April. Although that is the last rig of Pioneer's newbuild program, Mr Locke said, he's aware that industry-wide there is still a backlog of newbuilds to be delivered through the end of 2007.

"It does make for a difficult operating environment for land drillers," he said. "The market's moved more in favor of operators. Stacked rigs in every market allow them the opportunity to negotiate dayrates down, and gas prices aren't yet strong enough to absorb the existing rig fleet plus the newbuilds coming on."

ANOTHER TAKE

For **John Cromling**, executive vice president of drilling at **Unit Drilling**, he doesn't think "the remainder of the year will be any worse than what we've already seen."

He pointed out that post-winter, both the 1-year and 5-year natural gas prices are nearly identical to their levels in October 2006. "That's a positive sign indicating that concerns many people had before winter weren't quite so justified. I think the slump may not be as bad as what many had feared it would be," Mr Cromling said.



Bandera Drilling recently installed an Iron Derrickman on Bandera Rig 7. The West Texas area is experiencing some slow-down, said Ray Brazzel, president of the Abilene-based company.



Outlook for the rest of 2007 remains optimistic, said Jay Minmier, vice president - contracts and marketing for Grey Wolf. Above is Grey Wolf's Rig 511 in the Rocky Mountains.

As far as activities, he noted small decreases in almost all of Unit's operating areas except Eastern Oklahoma and Arkansas, fueled by the Woodford Shale and the Fayetteville Shale plays.

Unit added 6 new rigs to its fleet in 2006 and plans to add 4 more in 2007.

Jay Minmier, vice president - contracts and marketing for **Grey Wolf**, also said outlook for the rest of 2007 is optimistic, with commodity prices remaining strong, even though year-over-year drilling budgets are level. "Some operators are on pace to exceed last year's activity while others appear to have adopted a wait-and-see approach during the first quarter of 2007. As evidenced by recent permitting increases, we presume that some of this doubt has been erased."

Grey Wolf's customers also have shown satisfaction with value delivered by newbuilds, he added, and the company continue to find good opportunities for conventional rigs in all classes and depth ratings.

Grey Wolf focused on upgrades/refurbishments in 2006 and have "completely exhausted our inventory." The company delivered its first newbuild in November 2006

and has since fielded 3 more newbuilds, with 2 more expected to commence operations this year.

WEST TEXAS

In West Texas, **Ray Brazzel**, president of Abilene-based **Bandera Drilling**, said the area is experiencing "some slow-down" and seeing pressure on prices, with a flat 1st quarter 2007.

"But I think it's going to be OK. I don't see a big downturn. A lot of the pressure on prices is not because there's a big downturn, it's because so many more new rigs are coming on the market," he said.

Bandera recently put out its first rig with an Iron Derrickman to eliminate having a worker in the derrick. The company plans to install Iron Derrickman on 4 more rigs this year.

UNCONVENTIONALS

While land drillers haven't gotten much help from natural gas prices, operators' increasing focus on unconventional resource-

es — as evidenced by activity levels in the Woodford and Fayetteville shales — does continue to drive activity levels up.

Unconventional reservoirs are producing gas with very high depletion rates, which requires more and more rigs to drill more holes in order to keep production steady, Mr Locke said.

On the flip side, he continued, contractors can help operators on resources plays, or volume plays, covering a wide expanse of area that involves drilling the same type of well one after another. “Contractors can really help operators by providing rigs that move quickly, rig up quickly and drill fast. These more efficient operations make the resource plays much more financially rewarding for operators.”

ADVANCED TECHNOLOGY RIGS

Whether these unconventional plays are leading to strong operator preference for new advanced-technology rigs is unclear. According to Mr Cromling, it’s not the rigs — it’s the efficiency. “There’s no doubt that operators are being much more particular about the overall efficiency of the operation. That could be due to new technology, people, or a company’s business attitude,” he said. “I would be hesitant to say they prefer the new rigs specifically.”

Mr Locke agreed that older rigs also can perform very well, and he pointed out that the rigs being stacked out due to lack of work run across all classes of rigs, not just old rigs. “As long as a rig has been modernized and updated, it can perform efficiently,” he explained. “On more than 50% of Pioneer’s rigs, we installed brand-new, modern mud tank systems, and we’re adding triplex mud pumps on almost every one of our rigs. A rig with an original manufacturing date of 1980 can still be in excellent operating condition today.”

Mr Minmier echoed the sentiment, pointing out that the rig must complement the type of well work for operations to be at maximum efficiency. “Advanced technology wells often require advanced technology rigs. Our objective is to match the rig with the project, and we provide advanced technology rigs as needed. However, operators realize that technology does not supersede the human element. There is no reason why conventional rigs with strong, experienced crews can’t operate as safely and efficiently as newbuilds and, in fact, this occurs quite often. Clearly, there is meaningful, useful life remaining in the older rig fleet.”

He added that for some classes of older-generation land rigs, the return on capital invested through upgrading is superior to that of newbuilds. “It’s a similar equation to what we’ve seen in the offshore market with 2nd- and 3rd-generation MODUs.”

GLOBAL LAND DRILLING

Over the past 6 months, US-based **Parker Drilling** has moved 2 land rigs into South Texas on long-term contracts. However, that does not signify a return to the US land market, said **Robert Parker**, chairman, president and CEO of Parker Drilling. “It was an opportunistic move for 2 rigs coming off contracts in Mexico,” he said.

Rig 122 is doing both deep and horizontal drilling on Padre Island for **Kindee**, a subsidiary of an Australian company. Rig 256 is doing deep drilling in South Texas; upon completion, it will mobilize to southern Mexico for a term contract. “Land markets outside the US are healthier right now, primarily because they’re oil-driven, and oil prices have held up better



Whether an advanced technology rig or not, the human element remains a critical factor. "There is no reason why conventional rigs with strong, experienced crews can't operate as safely and efficiently as newbuilds," said Mr Minmier of Grey Wolf.

than natural gas prices," he said. Several of Parker's land rigs coming off of 3-year contracts are seeing "healthy dayrate increases."

Three rigs, including Rig 256, are going to southern Mexico. Parker is entering a new market with a 3-year subcontract in Libya. Two other rigs will mobilize from inactive status to work in Kazakhstan's Karachaganak Field. This will increase Parker's rigs operating in that field from 2 to 4 and extend the term of the 2 existing rigs under contract for 3 more years.

In 2006, the company ordered 4 land rigs from China. Two of these 2,000-hp, electric SCR rigs have already been delivered to Algeria under 3-year contracts in the Hassi Massoud area.

"The Middle East has been very strong both on land and offshore to pick up production capabilities. North Africa and parts of the former Soviet Union also are hot spots," Mr Parker said.

For his drilling contractor peers in the US, Mr Parker remarked that he believes companies will take this opportunity of slow activity and newbuild influx to let older rigs fall out: "Honestly I think the industry needs the new equipment." ♠