The Makonde tribe and liquid natural gas

DAVID TARIMO
@pwc_tz

Makonde watchmen were a common sight when I was a child; and if asked at the time what Mozambique and Tanzania had in common I would have probably referred to this ethnic group whose domain covers northern Mozambique and southern Tanzania.

Asked the same question today, and I would talk about the massive gas discoveries deep offshore that similarly straddle the two countries territories.

Mozambique's liquid natural gas (LNG) projects are well advanced in terms of moving to development – with the final investment decision (FID) on one project expected to be announced this month and the other expected in September. In both cases one can expect investment of between $20 billion to $25 billion.

January 2016 had seemed to be a turning point for Tanzania's potential LNG project with the current Government resolving a long outstanding issue in relation to location of the land for the LNG site – with a location identified in Lindi.

However, since then there appears to have been little traction in moving other aspects forward.

Earlier this year the President expressed his frustration with the slow pace and set a September deadline for finalisation of the first phase of negotiations.

The need for urgency is well articulated – not least, the resulting significant foreign exchange revenues and Government revenues would be welcome against a background of massive infrastructure spend and related debt commitments.

In terms of steps and timing, the next key milestone would be to agree a Host Government Agreement (HGA) setting out the commercial, fiscal and regulatory framework for the project.

Then, once the HGA is agreed work could start on Front End Engineering and Design (over say three years), following which a FID point would be reached; and if the decision was positive, then development would take a further five years.

It is important to note that significant economic benefits would accrue way ahead of the date of production. In particular, it has been estimated that the development phase (with investment of around $30bn) would add 2 per cent to the GDP growth rate.

Production Sharing Agreements (PSAs) entered into with international oil companies (IOCs) have been based on whatever model was in place at the time of negotiation – and when looking at the 2004, 2008 and 2013 model PSAs the trend in terms of terms has been for these to become ever tougher. The question of what is an appropriate split of take between the Government and the investor is a vexed one.

A 2014 report by an oil and gas consultancy firm when modelling the 2013 terms for an offshore gas project arrived at a much higher Government take as compared to Kenya and Mozambique respectively. Anecdotally it is understood that the last licencing round held in 2013, still at the height of the oil prices, and based on the new 2013 terms, received an unenthusiastic

response.

Ultimately there needs to be recognition of the need for an investor to make a commercial return commensurate with the risk undertaken. The high financial stakes become clear when one considers the offshore exploration expenditure ($2bn since 2010), the sums to be spent on development and the long delay until revenues are received.

The financial arrangements are just one part of the jigsaw puzzle that needs to be put in place for the LNG project framework.

Equally important are other regulatory matters – and in this regard it is no secret that extractive sector regulatory changes made in 2017 have caused quite a bit of angst in the investor community.

Given that Mozambique have already walked this path – hopefully we can learn from them, and thereby set a platform for more expeditious discussions between Government and the investors as to the fiscal and regulatory framework.

The nature of the LNG market is that projects are funded by up front long term customer supply contracts, and with the supply from potential LNG projects possibly exceeding future projected demand, there is a first mover advantage as not all potential projects will be able to move to development.

Additionally, as one looks forward past 2030, the expectation is that an ever increasing portion of global power needs will be met by alternative / green energy sources. Time stands still for no one – not even for askaris, as what once appeared to be the preserve of the Makonde has now been taken over by Maasai. So whilst there should not be undue haste in finalising agreements, we also do not necessarily have an excessive luxury of time.

David Tarimo, Country Senior Partner – PwC Tanzania. The views expressed do not necessarily represent those of PwC. For updates from PwC on tax and other matters, visit our website www.pwc.com/tz.