

Topic Du Jour

Quantifying the impact of the North Field East LNG project: potential winning bidders finally revealed

The Russia/Ukraine war has intensified the focus on LNG. After much anticipation, Reuters reports that according to sources, QatarEnergy has selected the winning bidders of the large (>\$30bn) NFE LNG project. Given acute sector focus on capex/FCF, we created an NFE project model to quantify the impact for XOM and COP.

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What's on our mind? After much anticipation and speculation, Reuters* has reported that QatarEnergy will announce that XOM and COP along with SHEL, TTE (covered by Lydia Rainforth) will be selected as working interest partners in its North Field LNG expansion project (NFE) with a combined working interest of 20 - 25%. Although the language is somewhat unclear, our interpretation and the basis for our analysis is that bids will cover the first four trains of the expansion (Phase 1), or ~32mtpa of LNG capacity. Chevron also submitted a bid to participate in the project but reportedly hasn't been selected. The announcement comes after initial invitations to bid in 2019, another round of bids in 2021, and interesting [reports**](#) in 2021 that returns offered to partners (8-10%) could be significantly lower than those offered for previous Qatar LNG projects (15-20%).

The Russia/Ukraine war has intensified investor focus on LNG as Europe looks to wean itself off of dependence on Russian natural gas and secure lower-risk long-term supply. Also, the resource scale and long-lived, low decline cash flows of the NFE LNG project mean that investor interest in Qatar's NFE partner decision has been high. For context, at full capacity the North Field East expansion will represent > 2.5x current US LNG export capacity and ~8% of Europe's total natural gas demand. In addition, historically Qatar LNG projects offered returns of 15 - 20%, and we estimate the NFE project would generate a ~20% return at strip assuming prior project fiscal terms ([see Figure 8](#)).

Thus, we built an NFE model (covering the first four expected trains, equivalent to 32mtpa) to examine the impact on capex and FCF of project participation for XOM and COP.

*[Qatar picks Exxon, Total, Shell, Conoco for mega-LNG expansion -sources](#), Reuters, 6/8/22

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| CORE

XOM	OVERWEIGHT
U.S. Integrated Oil & E&P	POSITIVE
Price Target	USD 111.00
Price (08-Jun-22)	USD 104.59
Potential Upside/Downside	+6.1%

Top Pick

COP	OVERWEIGHT
U.S. Integrated Oil & E&P	POSITIVE
Price Target	USD 132.00
Price (08-Jun-22)	USD 121.86
Potential Upside/Downside	+8.3%

U.S. Integrated Oil & E&P

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****Exclusive Energy majors bid for Qatar LNG project despite lower returns**, Reuters, 6/13/21

What we did: In order to assess the capex and FCF impact of participation in the project, we adjusted our NFE model to include a supplemental tax after the project achieves a cumulative IRR of 8%, which results in a full-life project IRR of 10% and is consistent with prior [headlines](#) of Qatar offering 8-10% returns. Although there have been conflicting reports, our analysis assumes 4 winning bidders (XOM, COP, SHEL, TTE) for Phase 1 (four trains) and apply an equal 6.25% working interest per partner. We first assume the project is 100% equity financed and that 100% of post capex cash flow is paid out to working interest partners. Lastly, given prior financing history for Qatar's LNG projects, we examine an alternative scenario in which the NFE project is instead financed with 75% debt at a 3% interest rate.

What's the conclusion? Given relatively low implied working interest for NFE (6.25% for each partner assuming total partner WI of 25%) along with the reported degradation in fiscal terms, we estimate the financial impact (capex and FCF) to XOM and COP is relatively limited. However, there are important strategic reasons that warrant involvement.

- See [Figure 1](#) for our annual capex forecast for the NFE project, [Figure 2](#) for our cumulative IRR projections, and [Figure 3](#) for our annual FCF forecast all on a 100% working interest basis and assuming Qatar imposes a supplemental tax. Also, see [Figure 8](#) for our estimate of NFE project returns based on prior (more favorable) Qatar LNG project terms.
- **XOM: Financial impact is limited, but confirms Qatar relationship.** For XOM, the financial impact is particularly limited given the company's scale. We forecast the capex and pre-return threshold FCF impact of NFE is 1% and 2% assuming 100% equity funding, respectively. However, we think XOM's participation confirms its ongoing partnership with QatarPetroleum (QP) after the company's Qatargas (QG) phase 1 contract was allowed to expire last year ([Left out in the cold - Potential impact of Qatargas' announced QG1 LNG contract expiration](#), 3/31/2021). We note that XOM and QP are also partners in the Golden Pass LNG export project in the US and exploration drilling in Cyprus. See [Figure 4](#) and [Figure 6](#) for our forecasted annual capex and FCF impact for XOM.
- **COP: Moderate potential financial impact but provides further E&P differentiation.** On a 100% equity basis we estimate that a 6.25% working interest in NFE would carry capex requirements that represent 3% of our total estimated capex during the build-out period (2022-2027) and 5% of FCF thereafter (prior to hitting the 8% IRR threshold). Alternatively, assuming 75% debt financing, the capex and FCF impact would be 1% and 4%, respectively. We can sympathize with an argument that COP would be better served by drilling significantly higher IRR, near term payback, wells in the Lower 48. However, we think COP's participation supports its longer-life, lower decline resource base, which is a differentiator among its E&P peer group. See [Figure 5](#) and [Figure 7](#) for our forecasted annual capex and FCF impact for COP.

Capex/FCF Implications for XOM and COP

Why it's different this time around

By all indications the North Field Expansion will follow a different playbook than the one followed for Qatar's prior LNG projects. Earlier North Field developments starting with Qatargas 1 in 1996 relied on IOC partners to assist with project design, finance and marketing. As a result, terms for prior developments were relatively favorable and included low royalty rates for associated condensate along with tax holidays.

However, QatarEnergy's technical and marketing capabilities have improved significantly, and the country's Minister of State for Energy was quoted in 2019 as saying that rather than needing partners for its NFE expansion, partners would be chosen based on value they could bring to Qatar ([Exclusive: Qatar shortlists partners for North Field expansion, but says it may go it alone](#), Reuters, 9/19/19). Later in 2021, Reuters reported that QatarEnergy would be offering potential partners "returns of around 8-10% in their investment" ([Exclusive Energy majors bid for Qatar LNG project despite lower returns](#), Reuters, 6/13/21). This level of return is significantly lower than prior Qatar LNG project returns of 15 - 20% and significantly lower than our estimated 20% NFE return based on prior project fiscal assumptions (see [Figure 8](#)).

Finally, combined partner interest for the NFE project of the reported 20 - 25% implies individual partnership interests of 5 - 6% assuming equal participation among the reported partners compared to XOM's 10 - 30% WI interest in prior projects, and COP's 30% WI in QG3. Recall that the entire NFE project will include six LNG trains (8 MMTA each). QatarEnergy invited oil majors to bid on the first four trains that comprise Phase 1 of the project, which is the basis of our analysis.

Reuters reports that QatarEnergy will hold a press conference and a signing ceremony on June 12, without specifying the subject.

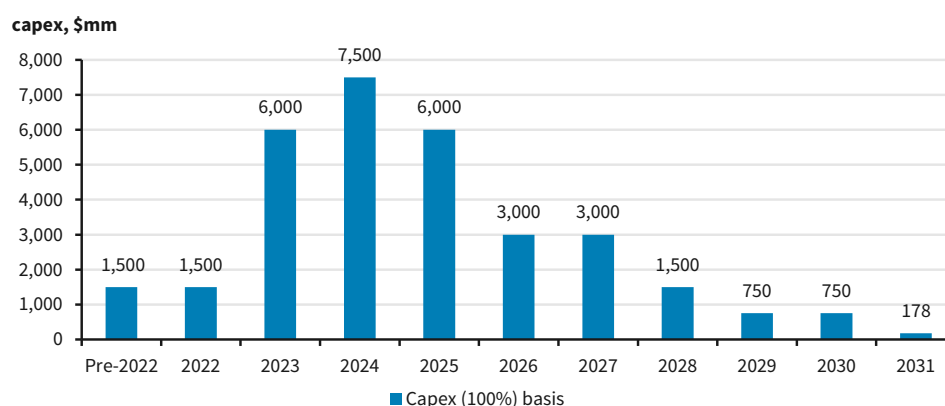
NFE modeling

In order to assess the potential financial impact to XOM and COP, we created a base case NFE model wherein we assume contractor returns will be limited to 10% through a supplemental tax after project returns hit an 8% IRR threshold. In addition, given limited information, we assume that each reported partner - Exxon, ConocoPhillips, TotalEnergies, and Shell - will participate at a 6.25% working interest.

Base case NFE estimates - 100% equity investment basis

Capex. Our NFE model includes total development capex of \$31.5bn, which accounts for ~5% inflation along with an additional \$1bn related to additional carbon mitigation infrastructure. In addition, we assume maintenance capex of \$0.10/mcf post project start-up.

FIGURE 1. NFE Phase 1 (4 trains): We forecast total pre-production capex of \$31.5bn on a 100% basis with capex peaking in 2024 at \$7.5bn

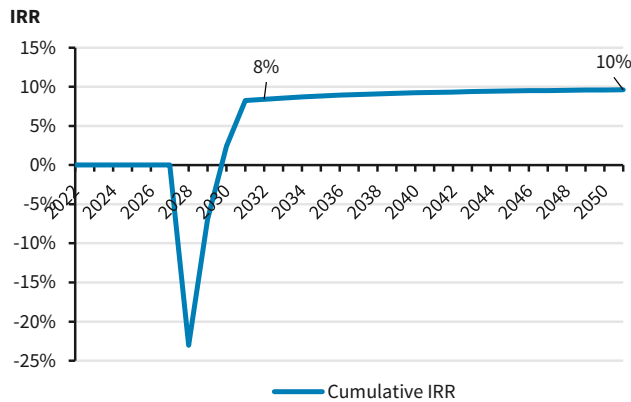


Source: Barclays Research, Company Reports, WoodMackenzie

Fiscal terms. Unfortunately there have been no indications on how fiscal terms will be adjusted to impose the reported 8-10% return limit on project partners. Therefore, our base case assumes terms consistent with prior Qatar LNG projects along with a supplemental tax of 95% that kicks in when project level returns reach 8%, and results in a full project life IRR of 10% at our \$78 Brent (2025 strip)/\$12 spot gas long term price. Our model suggests that partners hit the

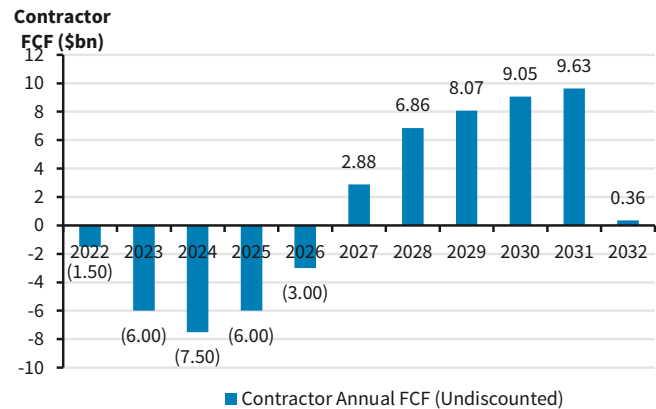
8% return threshold in 2031, resulting in strong near term cash flows that are then reduced to a nominal amount beyond 2030. See [Figure 2](#) and [Figure 3](#) below for details. We acknowledge that there could be a number of mechanisms to regulate partner returns, but given oil and natural gas price volatility, we assume that project partners would emphasize a near term/guaranteed return on investment.

FIGURE 2. NFE Phase 1: We estimate cumulative IRR reaches 8% in 2031...



Source: Barclays Research, Company Reports, WoodMackenzie

FIGURE 3. After which FCF to WI partners declines to <\$500mm



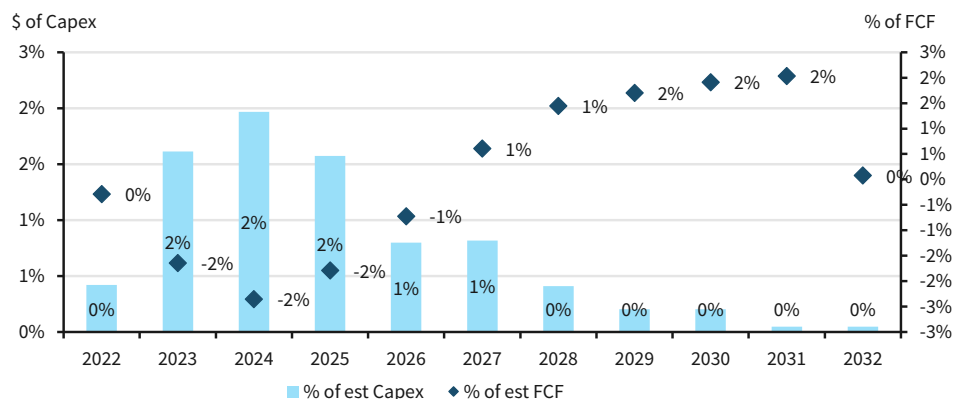
Source: Barclays Research, Company Reports, WoodMackenzie

Results

Our estimates at the company level assume that a 25% working interest in NFE is split equally between the four main reported partners. Thus, our base case model for XOM and COP is based on a 6.25% working interest in the project.

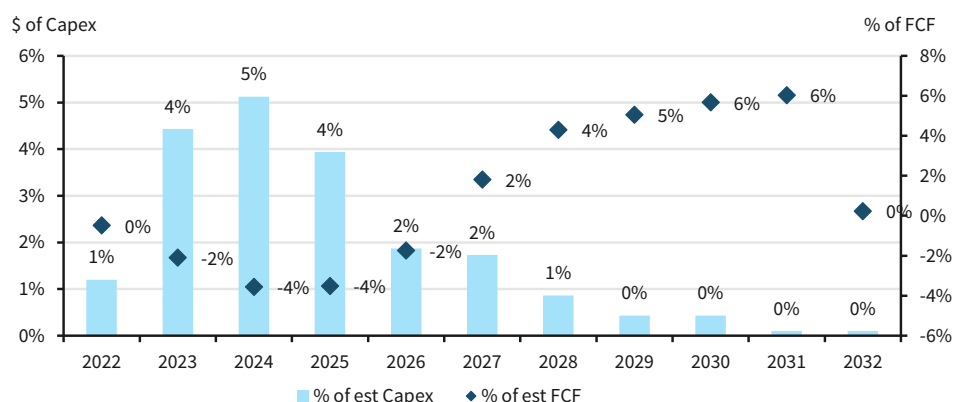
- XOM:** Assuming 100% equity financing, our model suggests that our assumed XOM 6.25% working interest participation in NFE would increase the company's total capex by 1% on average during the build-out phase between 2022 and 2027 and increase FCF by 2% after start-up (strip pricing), but prior to hitting the 8% return threshold in 2031 (<1% thereafter). Absolute capex during the build-out phase ranges between \$90-470mm/yr or ~\$280mm/yr on average. See [Figure 4](#).
- COP:** Assuming 100% equity financing, our model suggests that COP's participation in NFE at a 6.25% working interest would increase the company's total capex by 3% during the build-out phase on avg between 2022 and 2027, and increase FCF by 5% after start-up (strip pricing), but prior to hitting the 8% return threshold in 2031 (<1% thereafter). Absolute capex during the build-out phase ranges between \$90-470mm/yr or ~\$280mm/yr on average. See [Figure 5](#).
- Working interest still a moving target.** QatarEnergy hasn't made an official announcement on the winning bidders for the NFE project, and there has been conflicting news reports. Reuters reports one source indicates that XOM, SHEL, and TTE are expected to have around 20-25% in total of the offtake of the new project, while a second source indicates they are likely to get an offtake of one train each with COP sharing and additional train. In this case, the capex and FCF impact to COP will be even less than our estimate above given lower working interest. However, for the purposes of our analysis and for materiality, we assume that XOM, SHEL, TTE, and COP are the winning bidders of Phase 1 (four trains total) with an equal 6.25% working interest.

FIGURE 4. We estimate that a 6.25% WI in NFE Phase 1 would represent ~1% of XOM capex during the build-out period, and increase FCF by 2% after project start-up and prior to hitting the 8% return threshold



Source: Barclays Research, Company Reports, WoodMackenzie

FIGURE 5. We estimate that a 6.25% WI in NFE Phase 1 would represent ~3% of COP capex during the build-out period, and increase FCF by 5% after project start-up and prior to hitting the 8% return threshold



Source: Barclays Research, Company Reports, WoodMackenzie

Alternative case NFE estimates - 75% project financing

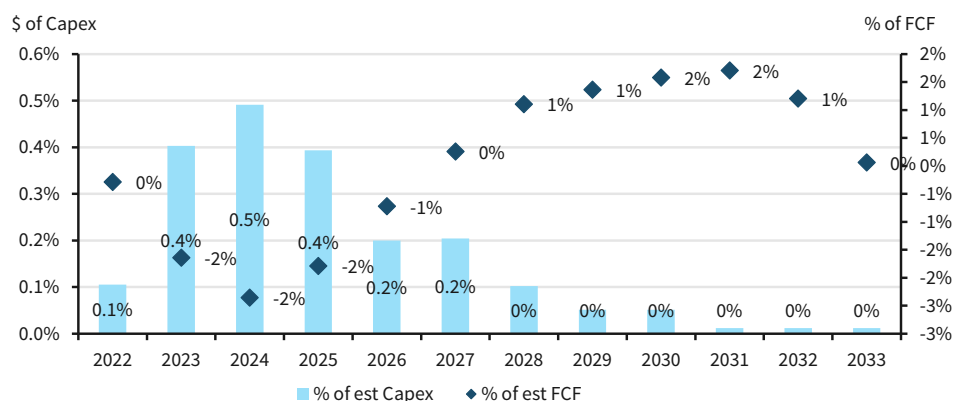
Similar to prior Qatar LNG projects, we expect that the NFE project may be partially debt financed. For example the QG4 project was 30%/70% equity/debt financed. As an illustrative case, we adjusted the model shown above to assume 75% project financing at a 3% interest rate with principal paid back ratably over the life of the project.

The cumulative impact of a relatively minor 6.25% equity stake and 75% debt financing significantly reduce the capex burden to equity partners. In addition, because we assume financing costs are incorporated into the project return calculation, the 8% return threshold isn't met until 2023 in our project finance case.

- **XOM:** In the 75% debt financing scenario, NFE capex would represent only 0.3% of our total XOM 2022 - 2027 capex forecast (vs. ~1% in the 100% equity financing scenario), while FCF after start-up would fall to 1% of total (vs. ~2% in the 100% equity financed scenario). See [Figure 6](#).
- **COP:** In the 75% debt financing scenario, NFE capex would represent only ~1% of our total COP 2022 - 2027 forecast (vs. ~3% in the 100% equity financing scenario), while FCF after

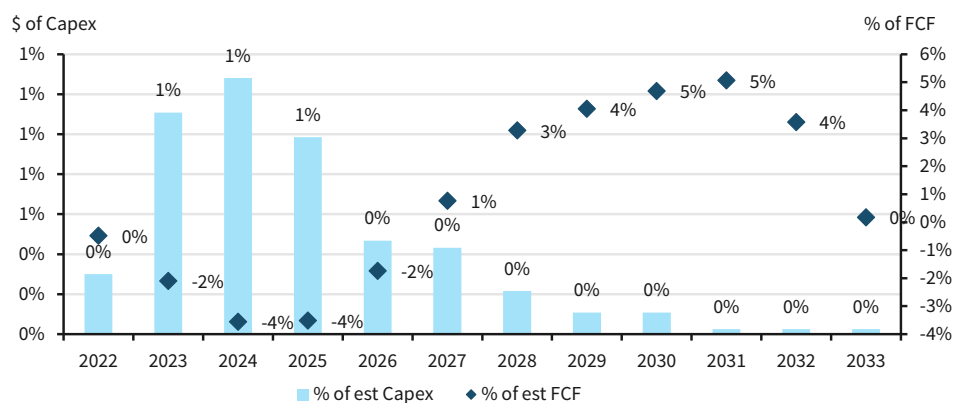
start-up would fall to 4% of total (vs. ~5% in the 100% equity financed scenario). See [Figure 7](#).

FIGURE 6. XOM: Assuming 75% project financing, XOM NFE Phase 1 capex falls to <0.5% of our total estimate during the build-out phase, and FCF would increase by 1% after project start up



Source: Barclays Research, Company Reports, WoodMackenzie

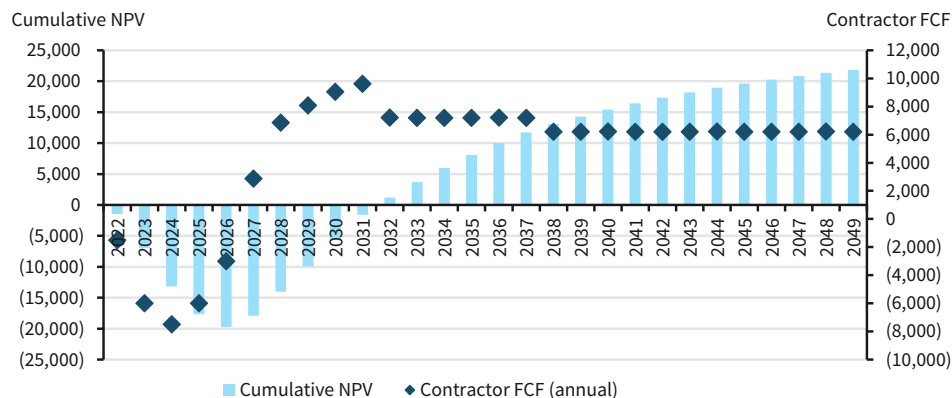
FIGURE 7. COP: Assuming 75% project financing, COP NFE Phase 1 capex falls to 1% of our total estimate during the build-out phase and FCF would increase by 4% after project start up



Source: Barclays Research, Company Reports, WoodMackenzie

Those were the days - NFE project returns based on previous (more favorable) Qatar LNG project fiscal terms

In order to show a baseline against the reported 8-10% returns offered to partners in the NFE project, below we show our estimated total project NPV and returns assuming the more favorable terms offered to partners in prior Qatar LNG projects. The cumulative estimated NPV of \$21.8bn equates to an IRR of 19.6% and cash flows after royalties and taxes remain above \$6bn even after DD&A exhaustion and tax holidays.

FIGURE 8. Estimated NFE Phase 1 value based on prior more favorable Qatar LNG project terms

Source: Barclays Research, Company Reports, WoodMackenzie

Investors likely anticipated CVX's unsuccessful bid

Unlike CVX, the reported winning bidders in Qatar's North Field expansion project are already participants in prior Qatar LNG projects. Moreover, with its existing presence and LNG growth prospects in the Eastern Mediterranean via its acquisition of Noble Energy's Israeli gas fields (Tamar and Leviathan) CVX may have been viewed as a potential competitor and/or less inclined to submit a competitive bid.

On its 1Q2'22 conference call CVX management noted that the company has recently increased gas exports to Egypt, and are in the process of assessing potential further production growth via increased natural gas penetration in Israel's power mix, distribution to countries in the region, as well as LNG export options (floating or via existing infrastructure in Egypt). As could be expected given European demand for non-Russian supply, our impression is that LNG and the Eastern Med have moved into a higher priority position for the company.

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ConocoPhillips (COP, 08-Jun-2022, USD 121.86), Overweight/Positive, A/CD/CE/D/J/K/L/M/N

Exxon Mobil Corporation (XOM, 08-Jun-2022, USD 104.59), Overweight/Positive, CD/CE/E/J/K/L/M/N

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Coterra Energy (CTRA)

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Exxon Mobil Corporation (XOM)	Hess Corporation (HES)	Marathon Oil Corporation (MRO)
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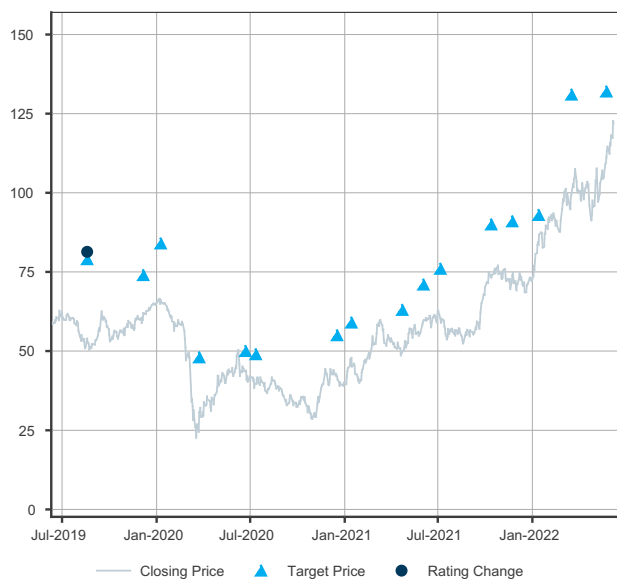
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ConocoPhillips (COP / COP)Stock Rating: **OVERWEIGHT**Industry View: **POSITIVE****USD 121.86** (08-Jun-2022)**Rating and Price Target Chart - USD (as of 08-Jun-2022)**

Currency=USD



Source: IDC, Barclays Research

[Link to Barclays Live for interactive charting](#)

Publication Date	Closing Price*	Rating	Adjusted Price Target
25-May-2022	109.48		132.00
18-Mar-2022	98.83		131.00
13-Jan-2022	84.40		93.00
23-Nov-2021	71.89		91.00
13-Oct-2021	73.23		90.00
06-Jul-2021	60.28		76.00
03-Jun-2021	59.47		71.00
23-Apr-2021	49.72		63.00
14-Jan-2021	47.87		59.00
17-Dec-2020	41.97		55.00
12-Jul-2020	39.69		49.00
22-Jun-2020	43.56		50.00
24-Mar-2020	30.74		48.00
09-Jan-2020	66.07		84.00
06-Dec-2019	61.97		74.00
19-Aug-2019	53.94	Overweight	79.00

Source: Bloomberg, Barclays Research

*This is the closing price referenced in the publication, which may not be the last available closing price at the time of publication.

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

A: Barclays Bank PLC and/or an affiliate has been lead manager or co-lead manager of a publicly disclosed offer of securities of ConocoPhillips in the previous 12 months.

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CE: Barclays Bank PLC and/or an affiliate is a market-maker in equity securities issued by ConocoPhillips.

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N: ConocoPhillips is, or during the past 12 months has been, a non-investment banking client (non-securities related services) of Barclays Bank PLC and/or an affiliate.

Valuation Methodology: Our \$132 price target represents 105% of our net asset value based on PDP value, estimated resource value, and a detailed valuation of each US shale development area.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks include execution on the company's lower 48 drilling program, and risks to long term viability of the TAPS pipeline. The ever-changing political landscape could also have an affect on company operations.

Exxon Mobil Corporation (XOM / XOM)

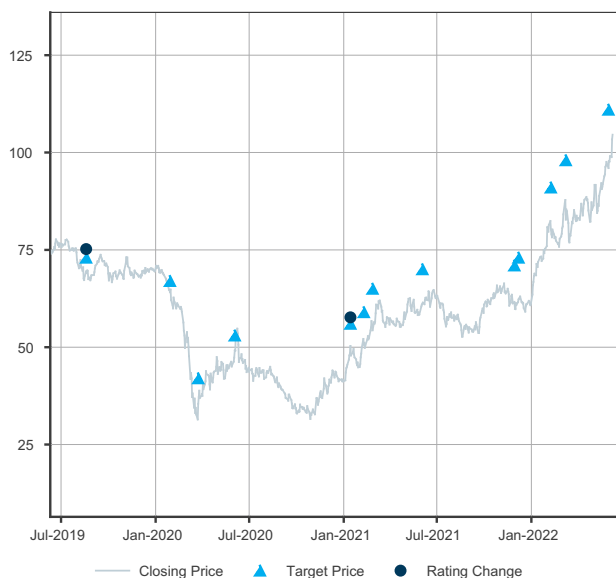
Stock Rating: **OVERWEIGHT**

Industry View: **POSITIVE**

USD 104.59 (08-Jun-2022)

Rating and Price Target Chart - USD (as of 08-Jun-2022)

Currency=USD



Source: IDC, Barclays Research

[Link to Barclays Live for interactive charting](#)

Publication Date	Closing Price*	Rating	Adjusted Price Target
31-May-2022	97.59		111.00
09-Mar-2022	87.78		98.00
08-Feb-2022	82.39		91.00

07-Dec-2021	62.27		73.00
29-Nov-2021	61.25		71.00
03-Jun-2021	61.18		70.00
26-Feb-2021	54.37		65.00
09-Feb-2021	50.63		59.00
14-Jan-2021	50.31	Overweight	56.00
03-Jun-2020	49.24		53.00
24-Mar-2020	35.44		42.00
29-Jan-2020	64.11		67.00
19-Aug-2019	69.45	Equal Weight	73.00

Source: Bloomberg, Barclays Research

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Valuation Methodology: Our \$111 price target is based on application of a 75 basis point premium to XOM's 2010 - 2019 1.3% yield premium to the S&P 500, or a total implied 3.4% dividend yield on estimated 2023 dividend of \$3.7/sh dividend.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to our price target include lower than anticipated commodity prices, operational issues associated with long lead time, highly technical development projects, and contract risk associated with production sharing contracts and licenses with sovereign governments.

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