

ID#070602

PUBLISHED ON
SEPTEMBER 4, 2007THE SANFORD C.
BERNSTEIN & CO.
CENTER FOR
LEADERSHIP AND
ETHICS CASE SERIES

Parker Petroleum in Jumandia

BY GEOFFREY M. HEAL*

ABSTRACT

Parker Petroleum has operated in Jumandia for 10 years. However, some opposition has developed to its new project, a refinery that is important to the company's growth. What issues should the company address when operating in a developing country? How should the company prioritize and address these issues?

CONTENTS

Introduction	1
Parker Petroleum.....	1
Jumandia Overview.....	2
Class Preparation	7
Exhibit 1	5
Assignment.....	7

* Paul Garrett Professor of Public Policy and Business Responsibility, Columbia Business School

Acknowledgements

This case was prepared with the writing and research assistance of Elizabeth Gordon, MBA '83, and Carolyn Whelan. Liav Abraham, MBA '09, assisted with the financial exhibits. Sandra Navalli MBA '03, provided guidance in the preparation of the case.

Copyright Information

© 2007 by The Trustees of Columbia University in the City of New York. All rights reserved.
The country, the company, and the characters in this case are fictitious, but are based on a composite of real entities and events. This case was prepared as a basis for class discussion rather than to illustrate either effective or ineffective handling of a business situation.

Introduction

Spirits were high at Parker Petroleum's annual shareholders' meeting. Year-end earnings were up almost 30 percent on soaring oil prices and buoyant demand for petrochemicals products in most markets.

But one decision weighed at the meeting's close and demanded action, if not resolution: What to do about Jumandia, a developing country near the equator where Parker had upstream and, soon, downstream operations? Locals were angry about prior instances of pollution; a situation that management wrongly assumed had long ago been resolved. And murmurs of discontent about natural-resource extraction were surfacing.

As a few U.S. representatives of environmental and indigenous organizations made their case to shareholders, the mood switched to one of concern. The question loomed. Should Parker go ahead with its plans for a new refinery there, and if so, what local issues should the company address?

Parker Petroleum

Parker was a U.S. oil company with production and refining as its two principal businesses. Based in Tulsa, Oklahoma, Parker started in the mid-1950s as a family-run firm and went public in the 1970s. Over that time Parker's revenue grew fourfold, a feat it duplicated by 2006, when annual sales were over \$19 billion. That year net income was just above \$7.5 billion.

Parker's post-millennium structure looked very different from its setup when it started. In fact, its key sources of revenue by region and by industry had shifted dramatically over the last 50 years. At its founding, Parker's domestic revenue had dominated results; today U.S. sales made up less than 60 percent of total revenue and were falling. And as demand for oil and its derivatives grew abroad and emerging markets became more attractive for drilling and local distribution, Parker's overseas operations expanded. The company moved into relatively untapped regions in Eurasia, Africa and Latin America, where local demand was growing. Today, those geographies were priorities.

PARKER IN JUMANDIA

Parker's current operations focused on oil exploration near Jumandia's rain forest, where it had operated for about 10 years through its prospecting and later its drilling activities in the interior. Refining would add a revenue stream with higher profit margins. As a result, Parker's board had recently approved plans for a 150,000-barrel-a-day refinery on the seacoast not far from the capital city. This would allow the company to capture the added value of refined oil products and would also supply Parker with a more defensive revenue stream should oil prices suddenly turn. The country's coastal location, management thought, also eased exports to developed countries. Construction of the refinery would require an investment of around \$4 billion. The Jumadian government and a majority of people in the country welcomed the imminent arrival of a new refinery, as it would create one to two thousand new jobs during the construction phase. In addition, the refinery was expected to provide at least 400 permanent positions and to help drive economic development in the area.

Jumandia Overview

Jumandia was a peaceful nation of nine million people and roughly the size of Maryland. Jumandia was colonized by the Portuguese in 1561 as a stopover en route to the Far East. Subsistence farming provided a livelihood for some families, while mines, fisheries and a logging industry in old-growth forests employed others. Oil drilling in the interior and a fledgling outsourcing industry also boosted income levels. Those jobs, Jumandia's small population and funding it received from multilateral banks helped literacy levels nudge 80 percent and fueled annual economic growth of 8 percent.

JUMANDIA POLITICS

Decades before its neighbors, Jumandia had shaken off its neocolonialist yoke in 1964 without bloodshed. Its subsequent transition to democracy in 1999 had been relatively smooth. Some said the one-party system was rigged, but regular elections occurred without upheaval.

In 2007, however, the political winds shifted. Despite the widespread popularity among Jumandians of President Anand Brathoon, an opposition party led by an outsider was mounting a campaign to unseat him. Sensing dissatisfaction among those citizens who acutely felt a growing wage gap between rich and poor, Adila Mapakse was luring those who said they were worse off. His three-pronged platform focused on protecting Jumandia's workers, environment and natural resources. His criticism of multinationals was particularly sharp. He tended to focus on oil companies, which he said had raided the country's natural resources and enriched themselves at the expense of local communities, which remained poor.

PARKER'S EXPERIENCE IN JUMANDIA

With minor exceptions Parker had been well received and was relatively successful in Jumandia. After extensive feasibility studies and government consultations, Parker had implemented its standard 30-year plan, which aimed to sow harmony in its new setting. It included shared school and medical facilities in Parker Village. The clinic provided free vaccinations via its Hospital to Home program. The program was run by a local NGO, which distributed these services around the country via bus and truck.

The company's relations with its local employees were generally positive. Foreign and Jumandian employees had integrated well. And though oil extraction and transport had been costly and complicated, the current field was producing well. Road building and pipeline laying had gone as well as could be expected. Some forest clearing had been required and had caused minor disruption of the local community, but reparations were later made.

In addition, about five years ago, some members of the indigenous Umati people had moved from a protected rain forest zone because they found unnerving the fumes, noise and gas flaring—wasted energy and unnecessary emissions, they pointed out—linked to nearby oil production. Financial amends were later made, but Parker's reputation for cultural insensitivity endured in some circles. Parker was also said to be cozy with President Brathoon, making the company easy prey for critics and competitors. The opposition exploited this, calling Parker a steamroller.

ENVIRONMENTAL CONCERNS

Parker was a natural target for Mapakse because of the alleged local impact of some of its activities. Contaminated water seemed to be the key culprit. Toxic runoff from Parker's exploration sites was said to have leaked

into rivers and watersheds—and a higher incidence of cancer among rural dwellers near those watersheds appeared to lend credence to those allegations. Furthermore, farmers and fishermen noted fewer kingfish, lily pads and waterfowl.

Parker said that it had long ago implemented watertight pipes and protective measures to prevent leaking and spills. Moreover, (at least internally) it said that industries backed by the Natural Resources Ministry, like mining, could have just as easily wrought such damage. So too could have overpopulation, sewage drain off or fertilizer runoff from intensive farming. Even sabotage wasn't out of the question. To appease the local community, Parker hired an expert to test for chemicals in streams and lakes. Studies conducted in 2004 were inconclusive.

INVOLVING THE COMMUNITY

In 2006, to defuse tension, Parker consulted citizens through public forums in churches and community centers. Parker's local staff also met with senior officials at the environmental ministry as well as leaders of Umati community groups. In these meetings, Parker proposed shared port facilities and a small-business development center. There was also talk of establishing an ecotourism buffer zone near the forest so that disruptions such as those experienced by the Umati would not occur again. The proposed programs would create local jobs and boost incentives to protect natural resources. Jumandia's representatives seemed amenable.

RISING UNREST

Elections in 2007 kept environmental issues on the front burner and shone a light on news that international groups and the media might normally have missed. Journalists were closely watching Mapakse's rapid rise, which was fueled by his movement's growing popularity and power.

Mapakse's words particularly resonated among the Ozani, a native people who lived near untouched swamps where Parker planned to build its new refinery. They worried about pollution, outside influence and losing their home. Mapakse's demands for environmental preservation also spoke to a fledgling ecological movement. New ecoventures wanted to keep Jumandia pristine, with a focus on protecting endangered mangrove species near the site of the new refinery. Finally, unions—formed in response to a rising disparity in income between those who worked on farms and in fisheries and more skilled laborers in the services industries—joined the critics in the opposition movement. They asked for higher wages, formal recognition of workers' rights and a public stake in natural-resource extraction.

At the same time, Jumandia registered on the radar screens of international oil firms. Its relative proximity to markets coupled with historically high oil prices seemed to justify the higher extraction costs that would be required to transport drilling gear and build roads to the undeveloped interior. The flurry of oil interest had also triggered talks between global investors and the government. Representatives of the China Petroleum and Chemical Corporation, known as Sinopec, had been spotted meeting with President Brathoon. Rumors swirled about a potential deal.

With major oil companies circling the globe in a search to replace dwindling oil reserves amid the rising risks of drilling in the Middle East, the attractiveness of Jumandia's resources could only increase. Thus, the Jumandian people's preoccupation with exploitation by outsiders would likely grow.

GROWING SUPPORT

Mapakse's followers multiplied as he spread his views through posters and personal visits to villages. Citizen activists from local environmental and indigenous organizations helped broadcast his message. The grassroots group Jumandians for Jumandia (J4J) also joined the movement. A more extremist group than the Umati, the members of J4J wanted the country to nationalize oil and push out all multinationals.

Mapakse's rhetoric became more militant as his movement tapped into international networks. Among them were Oil Change International (www.priceofoil.org) and Friends of the Earth (<http://www.foe.co.uk/index.html>), a UK-based NGO with campaigns against Shell and its operations in Nigeria. The Environmental Law Institute (www.eli.org), an NGO in Washington, D.C. that broadcast news about recent natural resource-related courtroom victories for marginalized groups, was also a part of these networks. ELI focuses on global incidents regarding pollution of protected areas.

Foreign citizen activists and celebrities followed. They included high-profile actors and musicians in the United States and Europe. Collectively, these groups demanded cleanup efforts, several million dollars in compensation to help cure illnesses associated with contaminated water and a share of Jumandia's oil wealth for Jumandians.

Finally, the socially responsible investment (SRI) community got involved. Among them were Citizens Funds (www.citizensfunds.com), a trailblazer among asset managers for the screening capabilities it had set up more than 25 years earlier.

Press reports and Citizens Funds' action alerts were prompting queries from investors and even Parker's shareholders about its activities in Jumandia. Journalists across the world said they would closely watch any talk or action related to the rain forest in Jumandia. NGOs and individual activists were also considering a blog and anti-exploitation text messages sent to mobile phones in Jumandia.

As management mulled over its options, some executives thought it might be wise to see how their peers had grappled with similar issues. Competitive intelligence could be gathered through newspaper articles, white papers and annual reports.

Exhibit 1

PARKER PETROLEUM INC. SUMMARY FINANCIALS (U.S. \$ MILLIONS)

INCOME STATEMENT

<u>Year Ending</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Total Operating Revenue	8,140	10,297	12,126	17,213	19,976
Cost of Goods Sold	3,629	4,287	4,860	5,968	6,912
Sales, General & Administrative	710	937	1,029	1,456	1,509
Interest Expense	<u>325</u>	<u>365</u>	<u>286</u>	<u>322</u>	<u>320</u>
Income Before Tax and other items	3,476	4,708	5,951	9,467	11,235
Taxes and other items	<u>2,388</u>	<u>3,028</u>	<u>3,126</u>	<u>3,658</u>	<u>6,635</u>
Net Income	1,088	1,680	2,825	5,809	4,600

BALANCE SHEET

<u>As of 12/31</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Assets					
Cash	161	751	1,319	2,407	1,473
Receivables	669	875	2,070	2,784	3,108
Inventory	540	538	600	788	908
Other Current Assets	<u>690</u>	<u>589</u>	<u>885</u>	<u>1,652</u>	<u>1,117</u>
Total Current Assets	2,060	2,753	4,874	7,631	6,606
Net Property, Plant & Equipment	14,340	15,382	16,096	18,888	26,748
Total Assets	16,400	18,135	20,970	26,519	33,354
Liabilities					
Accounts Payable	864	997	1,713	2,251	2,489
Other Current Liabilities	<u>1,595</u>	<u>1,782</u>	<u>2,053</u>	<u>2,449</u>	<u>2,707</u>
Current Liabilities	2,459	2,779	3,766	4,700	5,196
Deferred Tax	1,079	1,100	1,372	1,066	2,559
Long Term Debt	<u>4,397</u>	<u>4,393</u>	<u>3,680</u>	<u>3,161</u>	<u>2,881</u>
Total Long Term Liabilities	5,476	5,493	5,052	4,227	5,440
Total Liabilities	7,935	8,272	8,818	8,927	10,636
Shareholders' Equity	8,465	9,863	12,152	17,592	22,718
Total Liabilities and Equity	16,400	18,135	20,970	26,519	33,354

EXHIBIT 1 (CONTINUED)
PARKER PETROLEUM INC.
SUMMARY FINANCIALS
(U.S. \$ MILLIONS)

Year Ending 12/31	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Cash Flows from Operating Activities					
Net Income	1,088	1,680	2,825	5,809	4,600
Depreciation and Amortization	1,110	1,293	1,376	1,564	2,246
Other adjustments required to reconcile net income to cash flows from operating activities	<u>(685)</u>	<u>(275)</u>	<u>(756)</u>	<u>(1,653)</u>	<u>2,626</u>
Cash Flows from Operating Activities	1,513	2,698	3,445	5,720	9,472
Cash from Investing Activities	(1,068)	(2,104)	(2,165)	(4,113)	(10,127)
Cash from Financing Activities	(502)	(4)	(712)	(519)	(279)
Increase (decrease) in cash and cash equivalents	(57)	590	568	1,088	(934)
Cash and cash equivalents:					
Opening Balance	<u>218</u>	<u>161</u>	<u>751</u>	<u>1,319</u>	<u>2,407</u>
Cash and cash equivalents:					
Closing Balance	161	751	1,319	2,407	1,473

Class Preparation

Please prepare a response to the following question for class:

What issues and stakeholders should Parker address and why? Are there any opportunities for local communities and/or the environment to benefit from Parker's presence? Can Parker's bottom line benefit from any of these opportunities?

During class, you and your learning team will be asked to identify, analyze and prioritize these stakeholders and issues using the "2 x 2" mapping framework described in the "Introduction to Corporate Social Responsibility" paper in your Orientation materials.

Assignment

The following questions are to be researched and answers prepared after class. Given your team's time constraints, a limited number of sources should be used to refine your team's analysis. As a rough guide, teams should spend no more than 45 to 60 minutes accessing library resources.

The board asks you to further investigate these issues and learn from what other companies in this industry have experienced in developing countries.

1. Which are the comparable companies in this industry?
2. Find three relevant articles or reports to support and refine your "2 x 2" issues analysis.
3. What issues are highlighted by corporate social responsibility analysts and research providers?

SUBMISSION INSTRUCTIONS

1. Please provide a one-page summary responding to the questions above for presentation to the board on Friday, August 24. (These will be collected by your peer advisor at the end of this session.)
2. Attach your "2 x 2" map (a handwritten version is acceptable).
3. Write your names and cluster at the top of the page.