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CNOOC engages with canadian stakeholders[[1]](#endnote-1)

Professor Klaus Meyer and Alexandra Han wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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In 2013, China National Offshore Oil Corporation (CNOOC) acquired Canadian oil exploration company Nexen for US$15.1 billion in the largest-ever acquisition abroad by a Chinese company.[[2]](#endnote-2) For the Canadian public, the acquisition was controversial from the outset, and CNOOC experienced unfamiliar public scrutiny during the process of approval by the Canadian and U.S. authorities.

After the deal was completed, Nexen’s operations were not smooth. Operating costs exceeded budgets, and, when the oil price sharply declined, Nexen came under considerable pressure because its exploration sites were primarily in high-cost locations, such as Canadian oil sands. Consequently, Nexen had to handle challenging questions from its Chinese owners and other interested parties. In July 2015, Nexen was in the news again because a pipeline leak spilled five million litres of oil emulsion in a remote area.[[3]](#endnote-3) Then, after that media storm had settled, in January 2016, a worker died and another was hospitalized after an explosion in an oil cracker facility.[[4]](#endnote-4) Nexen’s management team had to respond to media enquiries but also faced broader questions regarding its internal processes and its corporate strategy.

China’s Quest for Resources

In 2010, the Chinese government started promoting a “going-out strategy” of encouraging large enterprises to invest overseas to access resources, technologies, and markets. Energy security was of particular concern because the fast-growing Chinese economy was increasingly dependent on imported energy and other natural resources.[[5]](#endnote-5) At the time, global oil markets experienced volatile but generally high price levels due to increasing demand from emerging economies. The benchmark West Texas Intermediate (WTI) index averaged at $94 per barrel, while the Brent index averaged at $111 per barrel.[[6]](#endnote-6) China imported oil from Russia, the Middle East, and Africa, but with rising demand at home, it was looking elsewhere to secure its resource needs.

As Chinese resource companies were looking to secure access to natural resources around the world, they found Canada a potentially attractive business partner due to its rich natural resources, energy security, and advanced science and technology. Moreover, an operation in Canada could potentially access not only rich natural resources but also professional management and experienced staff.[[7]](#endnote-7) At the same time, Canada offered a relatively stable political environment and was thus considered “a safe place to invest.”[[8]](#endnote-8)

China National Offshore Oil Corporation

The CNOOC Group was established in 1982 under the central government of China, focusing on the exploration and development of oil and gas, especially in offshore China and overseas. In 1999, the CNOOC Group established CNOOC Ltd. in Hong Kong as its international holding company (see Exhibit 1). CNOOC Ltd. was listed on the Hong Kong (stock code CNOOC) and New York (stock code CEO) stock exchanges in 2001, raising $1.25 billion in the initial public offering.[[9]](#endnote-9) By the end of 2015, five subsidiaries of the CNOOC Group had gone public: CNOOC Ltd., China Oilfield Services Ltd., Offshore Oil Engineering Co., Ltd., China BlueChemical Ltd., and Shandong Haihua Group Co., Ltd.[[10]](#endnote-10)

CNOOC Ltd. first attracted international attention in 2005, when it bid to take over the Californian oil and gas firm Unocal for $18.6 billion but later withdrew its bid due to political opposition in the United States. Its first major acquisition in the United States came in 2010, when CNOOC paid $1.08 billion for a 33 per cent stake in the Eagle Ford Shale Project in Southwest Texas, jointly owned with Chesapeake Energy Corporation.[[11]](#endnote-11)

CNOOC Ltd. achieved major breakthroughs in both shallow and deepwater exploration, and its reserve replacement ratio reached 112 per cent in 2014, with net proven reserves of 4.48 billion barrels of oil equivalent (BOE) and production of 1.18 million BOE per day (b/d).[[12]](#endnote-12) In 2015, the CNOOC Group climbed to 72nd place in the Fortune Global 500, with total assets of ¥1,164.2 billion. It had become one of the largest oil and gas producers in China, and had diversified in related industries such as oilfield development, the refining and marketing of petroleum, and power generation.[[13]](#endnote-13)

In 2011, the CNOOC Group published its “Second Leap Forward Development Strategy.” Its strategic objective was to grow the core oil and gas business by accelerating growth in liquefied natural gas (LNG) and coalbed methane (CBM) and by expanding oilfield professional services, petroleum sales, and oil trade. In addition, CNOOC aimed to develop related businesses, such as oil refining, chemicals, financial services, and alternative energy. Its ambition was to become a globally leading energy company by 2030. The plan envisaged doubling oil and gas production within a decade, and tripling annual output from 2010 levels by 2030. At the same time, CNOOC committed to corporate social responsibility, aiming to become a role model as a responsible national oil company.[[14]](#endnote-14)

Nexen and Long Lake Oil Sands

Nexen originated from Canadian Occidental Petroleum Ltd. (CanOxy), an oil and gas producer headquartered in Calgary since 1971. In the 1980s and 1990s, it acquired oil and gas exploration projects in the Gulf of Mexico, Yemen, and the North Sea. Renamed Nexen in 2000, it launched several ambitious investment projects, notably the Buzzard offshore facility in the British North Sea and Long Lake oil sands exploration in Alberta, Canada.[[15]](#endnote-15) In the early 2000s, Nexen was one of the most admired companies in Alberta, respected not only for its technological prowess but also for its environmental responsibility and its employee care.

Oil sands were considered an attractive alternative source of energy in view of rising oil prices and new extraction and refining technologies that became available in the early 2000s. However, they were also controversial, as environmental groups criticized the contamination of the land caused by the extraction of oil from oil sands. Nexen’s Long Lake project, about 75 kilometres south of Fort McMurray in Northern Alberta, applied new technologies that reduced the environmental impact of oil sand extraction by steam-assisted gravity drainage (SAGD) processes that reduced carbon emissions and by the use of mainly recycled water.[[16]](#endnote-16) In 2003, Long Lake received regulatory approval and in 2006, construction of the facilities was completed. In 2007, the injection of steam into the well pads began; in mid-2008, SAGD bitumen processing started; and, in 2009, production of premium synthetic crude oil began.[[17]](#endnote-17) In 2009, Nexen acquired an additional 15 per cent interest in the project from its partner Ormat Process Technologies Inc. (OPTI), increasing Nexen’s ownership stake to 65 per cent and taking operational responsibility for the project.[[18]](#endnote-18)

However, the project encountered technical problems and engineering missteps from the outset and failed to meet production targets. Rather than the projected 280,000 b/d, Long Lake produced only 30,000 b/d in 2011.[[19]](#endnote-19) Some problems arose from the nature of the oil deposits: uneven deposits interspersed with shale made penetration more difficult, leading to vast variation in ore quality across locations. Moreover, high water saturation levels made the oil sands at Long Lake hard to tap. Other problems arose from technical incidents that caused costly delays in the construction.[[20]](#endnote-20) For example, Nexen skipped the conventional on-site pilot project and instead moved directly to a large-scale commercial operation. Thus, wells were drilled close to the site’s base plant to save time and money, but the wells quickly became saturated with water and were far from the richest deposits of crude, requiring more steam than planned. This increased construction costs from an initial project budget of $2.6 billion to more than $6.1 billion by 2007.[[21]](#endnote-21)

Due to its focus on locations where the extraction of oil was technologically challenging, Nexen’s operating costs were much higher than those of other major oil exploration companies. In 2011, Nexen pumped about 200,000 b/d at a cost of $20.84 per BOE. In contrast, CNOOC’s average cost per BOE was $9.01, somewhat lower than that of Chinese competitors PetroChina ($11.54) and China Petroleum & Chemical Corp ($15.43). Global competitors faced similar cost conditions at $9.44 for Exxon Mobil and $10.78 for Royal Dutch Shell.[[22]](#endnote-22)

OPTI, Nexen’s partner, ran into financial difficulties as a consequence of the challenges at Long Lake. By 2011, it had $2.8 billion of debt and not enough cash on hand to meet even its 2011 interest payments.[[23]](#endnote-23) Moody’s cut its ratings on some of OPTI’s debt to Caa-3. At this stage, CNOOC took over OPTI, thereby acquiring an equity stake in the Long Lake project.[[24]](#endnote-24)

The poor performance of the Long Lake project undermined Nexen’s financial performance, and its stock price dropped 20 per cent from 2009 to 2012. In January 2012, Marvin Romanow stepped down after 13 years as chief executive officer (CEO). Chief Financial Officer Kevin Reinhart was appointed as interim CEO.[[25]](#endnote-25) In 2012, the performance deteriorated further as net income fell to $333 million, down 53 per cent from the previous year.[[26]](#endnote-26) The poor financial performance led to speculation that Nexen would become a takeover target.

Political Controversy

In July 2012, CNOOC Ltd. made an offer to acquire Nexen for $15.1 billion ($27.5 per share) in cash, a premium of 61 per cent over the previous day’s trading price.[[27]](#endnote-27) Nexen offered advanced technology and expertise, which Chinese companies were seeking to use both at home and throughout their increasingly global operations. In addition to the oil sands operations, Nexen had assets in offshore production and reserves in the North Sea, the Gulf of Mexico, Western Africa, and Yemen, which would help CNOOC to diversify its asset portfolio geographically.[[28]](#endnote-28)

However, completion of the deal depended on approval by the government of Canada. The Canadian foreign takeover law required investors to demonstrate a “net benefit” for the nation. This review was a serious matter: in October 2012, the government rejected a bid of $5.2 billion by Petroliam Nasional Berhad (Petronas), Malaysia’s state-owned oil company, for Progress Energy Resources. CNOOC also needed approval from authorities in the United States because of Nexen’s assets in the Gulf of Mexico, and from authorities in the European Union and China.[[29]](#endnote-29)

Having learned from the Unocal experience in 2005, CNOOC hired professional advisors in Canada to support it during the process. CNOOC signalled early to key policy-makers that it intended to make a major deal so they were not surprised and would not make early media statements based on insufficient information. CNOOC also worked early and proactively on the commitments it would make to demonstrate the net benefit to Canada, the criterion established in Canadian foreign investment law.

The Canadian government under Prime Minister Stephen Harper of the Conservative Party actively encouraged foreign investors. Harper saw it as a “national priority” to boost economic growth by diversifying exports away from the U.S. market and selling more resources to Asia.[[30]](#endnote-30) Similarly, Alberta Premier Alison Redford considered the CNOOC–Nexen deal as “an important investment for Alberta and for Canada.”[[31]](#endnote-31) For a long time, the United States had been Canada’s only major customer, yet in the 2010s, oil production was increasing in the United States. At the same time, Canada lacked the capital to develop its natural resources alone and needed overseas investment.

For these reasons, the business and investor community generally viewed the deal favourably. However, among political commentators in Canada, the CNOOC–Nexen deal triggered lively debate. People were concerned not only about the ownership of Canadian natural resources by a foreign state-owned enterprise (SOE), but also about doing business with a company owned by a non-democratic state. For example, opposition leader Thomas Mulcair of the New Democratic Party expressed reservations:

We’re very concerned about the potential sale of a strategic Canadian asset, not only to a foreign enterprise, but one that is wholly controlled by a foreign government that doesn’t follow the same market rules as Canada . . . . The question is how can it be in Canada’s interest, how can it be of a net benefit to Canada, to sell a strategic natural resource to a corporation that is wholly owned by a foreign country?[[32]](#endnote-32)

A public opinion poll suggested that 58 per cent of Canadians believed the government should block the Nexen takeover.[[33]](#endnote-33) Members of Parliament for the governing Conservative Party reported letters from voters calling for rejection of the deal, and they heard reservations in conversations with their own supporters. One Conservative member of Parliament speaking to the media on condition of anonymity summarized the sentiments: “On paper, it looks like a good exchange that will bring wealth and growth to this area. . . . However, the other side of the coin is the fact that it is a state-run enterprise, a government-owned company. That’s what’s causing the apprehension.”[[34]](#endnote-34)

An expert on Canadian foreign investment law, top-tier government official Paul Boothe, assessed the situation:

When you look at what they’ve said about their plans in terms of investment, in terms of employment, in terms of governance, in terms of social things like corporate responsibility—all of those things are consistent with the criteria in the Investment Canada Act. . . . [However,] there are some bigger questions: Should we have state-owned enterprises investing in Canada? How much from a certain country? How much from China? . . . In my view, those are discussions about the rules themselves rather than discussions about the application of the current rules for this particular deal.[[35]](#endnote-35)

Similarly, scholarly observers interviewed by the media varied in their assessment. For example, China-born economist Duanjie Chen of the University of Calgary’s School of Public Policy argued that

Chinese SOEs are unlike Crown corporations in Canada in that they do not operate on market principles. It should not be allowed to become an instrument in China’s distorted and often disreputable drive toward global hegemony. Chinese government use of state-owned enterprises has contributed to lower priority on human rights, the environment, social justice, and corporate rectitude.[[36]](#endnote-36)

In contrast, Yuen Pau Woo of the Asia Pacific Foundation called Chen alarmist in her criticism, saying:

The government should treat all foreign companies operating in Canada equally. I’m sure we can find examples of malfeasance of Chinese SOEs, but we can probably find examples in the private sector as well. The real question is—do we have the ability in Canada to either prevent that from happening or impose remedies . . . for say polluting a fresh source of water? The answer surely is yes.[[37]](#endnote-37)

On the Chinese side, CNOOC remained publicly optimistic throughout the approval process. The Chinese authorities described the deal as a litmus test for how open Canada was to Chinese investment, particularly from state-owned companies and those in the resources sector. Chinese diplomats suggested that rejecting the deal might cause a serious rumple in the Canada–China relationship, with a negative impact on future Chinese investment in Canada.[[38]](#endnote-38) CNOOC made extensive commitments to demonstrate the net benefits of the deal, including the following: (1) half of all board and management positions were to be held by Canadians, (2) the employment level would be maintained for at least five years, (3) Nexen’s headquarters would remain in Calgary, (4) CNOOC itself would be listed on the Toronto Stock Exchange, and (5) CNOOC would continue Nexen’s social responsibility and investment plans.[[39]](#endnote-39)

Because of the public controversy, the Canadian government extended its review of the deal twice.[[40]](#endnote-40) Eventually, Prime Minister Stephen Harper approved CNOOC’s takeover of Nexen on December 8, 2012. At the same time, the Canadian government announced that it would prohibit future acquisitions by state-owned companies in the oil sands industry barring exceptional circumstances. This new policy made foreign investment in the Canadian natural resource sector more difficult. However, Stephen Harper emphasized that “foreign state-owned business will still be welcome to acquire minority stakes and enter into joint ventures with Canadian businesses.”[[41]](#endnote-41)

After the Canadian and European approvals, the deal had one final hurdle—approval by the Committee on Foreign Investment in the United States (CFIUS), which was necessary due to Nexen’s assets in the Gulf of Mexico. This approval was finally received in February 2013; according to media reports, CNOOC agreed to surrender operating control of assets in the Gulf of Mexico to accommodate U.S. national security concerns.[[42]](#endnote-42)

The Integration of CNOOC and Nexen

With the completion of the deal, CNOOC’s worldwide oil production increased by 20 per cent and its reserves by 30 per cent, and it gained access to state-of-the-art shale gas and deepwater expertise.[[43]](#endnote-43) Following the agreed conditions, CNOOC retained the top management team and the workforce of Nexen. Kevin Reinhart, who had been CEO of Nexen since January 2012, continued as CEO, while Li Fangrong, CEO of CNOOC, became non-executive chairman. Other members were Barry Jackson, Thomas O’Neill, and William Berry.[[44]](#endnote-44)

The initial post-acquisition strategy envisaged Nexen as a fairly autonomous subsidiary. In a media interview in February 2013, Li Fangrong said:

Basically we are not changing anything. Nexen has been proven to be a very successful company. Why would we change it? I am not expecting to change the way Nexen manages the business. So basically, everything stays as usual, other than that Kevin now reports to me, and before he reported to the board. From time to time, we will have interaction between here and the Beijing headquarters.[[45]](#endnote-45)

However, at a strategic level, CNOOC recognized the need to improve the financial performance of Nexen while stabilizing its workforce. CNOOC president, Yang Hua, announced, “The company is to integrate the planning, finance, exploration, and development departments of the two companies over the next three or five months.”[[46]](#endnote-46)

The integration started in March 2013 with the delisting of Nexen from the New York Stock Exchange. In May, CNOOC started to partly repay a $6 billion short-term bridge loan it had used to finance the acquisition by selling $4 billion of corporate bonds in the biggest dollar-denominated offering from Asia outside of Japan. The premium CNOOC paid was 35 basis points less than on similar-maturity securities it had issued in 2012.[[47]](#endnote-47) In September 2013, CNOOC Ltd. began trading on the Toronto Stock Exchange, fulfilling a condition of its acquisition of Nexen.[[48]](#endnote-48) CNOOC exceeded its production target for 2014 with a net production of 4.4 billion BOE and an average daily net production of 1.1 million BOE—a 20.6 per cent increase over the previous year. With the contribution of Nexen, CNOOC’s reserve replacement ratio reached 327 per cent.

CNOOC integrated some aspects of Nexen through its foreign capital operation system, technology sharing, and cultural integration. CNOOC established an independent office for overseas health, safety, and environment management and introduced its global crisis management system to Nexen, which included coordinated emergency response teams and joint emergency drills. Information technology systems were connected through an information-sharing platform and a special network connection between Beijing and Calgary for live telephone conversations, video meetings, email address list integration, and safe transfers of large files.[[49]](#endnote-49)

In the area of social responsibility, CNOOC continued Nexen’s community projects in Canada, the United Kingdom, and the Gulf of Mexico. In 2013, CNOOC donated $3.1 million to support community infrastructure and flood relief projects in Canada. Employees of Nexen contributed 1,900 hours of post-disaster reconstruction and volunteer services.[[50]](#endnote-50)

Honeymoon over?

After a promising start, CNOOC soon ran into a variety of challenges in its new Canadian operations; operating costs were exceeding budgets, especially at Long Lake, while a plummeting oil price undermined the financial viability of high-cost oil exploration projects. Thus, the financial performance of the CNOOC Group suffered from Nexen’s cost structure. While oil and gas sales grew by 15.4 per cent, costs rose even faster. Consequently, net profits declined 11.4 per cent, primarily due to increasing operating and exploration costs, and a decreasing oil price. By the end of 2014, production climbed to 1.18 million b/d (an increase of 5.1 per cent) of which Canadian production accounted for 5.3 per cent. However, operating expenses increased ¥31.2 billion, of which operating expenses in Canada accounted for 19.8 per cent.[[51]](#endnote-51) Despite huge investments, Nexen could not be turned around, and in 2015, Nexen’s operational loss widened to ¥2.1 billion (all data calculated from Exhibit 2).

Nexen’s financial challenges got worse when crude oil prices plunged from $110 per barrel in early 2014 to less than $60 at the end of the year (see Exhibit 3). Throughout 2015, the price remained low due to concerns over global economic prospects and an excess global supply of crude oil. In 2015, the WTI crude oil price averaged $48.67 per barrel, and the Brent crude oil price averaged $52.32 per barrel.[[52]](#endnote-52) Consequently, CNOOC’s consolidated net sales slipped by 33 per cent to ¥146.6 billion in 2015. The Canadian subsidiary was even more affected, with net sales dropping by 53 per cent to ¥5.0 billion.[[53]](#endnote-53) However, Nexen was not the only one that suffered; the Alberta oil industry experienced massive downsizing. Some foreign operators shut down their entire extraction activities and laid off most of their employees, leading to a sharp increase in unemployment in the province.

In 2012, CNOOC had bought Nexen for $15.1 billion when the oil price was high. Yet, by 2015 many of its assets were worth far less, and CNOOC faced a write-down estimated to be at least $5 billion.[[54]](#endnote-54) With an oil price of $50, the exploration of the oil sands—a relatively high-cost source of oil—was no longer financially attractive. Analysts of BMO Capital Markets estimated that Nexen’s supply costs, a measure of break-even price plus a return on capital invested, were $76.5 per barrel and, at its Long Lake project, as high as $188.50.[[55]](#endnote-55)

Attempting a Turnaround

The oil price slump and high operating costs forced a rethinking of CNOOC’s global operations. CNOOC headquarters in Beijing reviewed all aspects of business, reduced capital spending, and took more direct control of Nexen. In particular, the business development unit was centralized in Beijing to enable better coordination of investments around the world.[[56]](#endnote-56)

However, this plan led to tensions between CNOOC leaders in Beijing and senior management in Canada, who intended to continue running Nexen as an autonomous business unit.Consequently, in April 2014, Reinhart was replaced by Fang Zhi, an executive vice-president of CNOOC with a career of 30 years in the company, who had played an instrumental role in negotiating the Nexen acquisition in 2012 and served on Nexen’s board of directors.[[57]](#endnote-57) Moreover, in November, Nexen dismissed four vice-presidents of its finance division.[[58]](#endnote-58) CNOOC had originally committed to the Canadian authorities to keep 50 per cent of the leadership team Canadian, yet this commitment needed to be reassessed due to the changing market environment.

In 2015, to adapt to these changing market conditions, CNOOC strengthened cost control, promoted regional development of oil and gas, and pushed cutting-edge offshore engineering, drilling, and production technologies to operations. In a press release, Nexen announced the layoff of 340 employees in North America and 60 in the United Kingdom. Canadian politicians called for close scrutiny of CNOOC’s compliance with its commitments made to the Canadian government, and Nexen stated that it was “fully compliant with all of its Investment Canada undertakings” (see Exhibit 4).

CNOOC cut operating expenses around 9 per cent group-wide and 30 per cent in Canada. Operating expenses per BOE decreased 20.9 per cent to $9.55, while exploration expenses were reduced by 14.1 per cent to ¥9,973 million.[[59]](#endnote-59) Capital expenditures were reduced by 30 per cent to ¥67.7 billion in 2015, and were expected to be cut further to no more than ¥60 billion in 2016.[[60]](#endnote-60) Since 2013, Nexen’s headcount had been reduced by about 300 from an original 3,000 employees.[[61]](#endnote-61)

Safety and Environment Incidents

On July 15, 2015, Nexen discovered a pipeline leak that spilled about 315,000 barrels (five million litres) of heavy crude mixed with sand and water near its Long Lake facility.[[62]](#endnote-62) The leak was from a brand new pipeline about 40 kilometres south of Fort McMurray in a rural area surrounded by boreal forests. Initial investigations suggested that the leak began sometime between June 29, when crews finished cleaning the pipeline, and July 15, when a contractor discovered it.[[63]](#endnote-63) Nexen activated its emergency response plan and immediately started a cleanup operation. The Alberta Energy Regulator worked with Nexen from the outset to ensure the safety of the site and to investigate the cause of the accident.[[64]](#endnote-64)

On July 17, Nexen invited the media for a tour of the cleanup operations. The site was fenced off during the cleanup efforts, and plastic eagles had been set up to deter wildlife from the area. About 130 workers were on the site, working to contain and vacuum the spill. Nexen CEO Fang Zhi publicly apologized for this incident during the site tour:

It’s disheartening to see the site here, and it is disappointing that this has happened. I therefore personally apologize for the consequences this may have caused. But our purpose today, really, is to be open and transparent with the public. Our focus as of now is ensuring the safety of our workers on the site, minimizing whatever impact on the environment and the wildlife, as well as understanding the root causes of the incident through investigations.[[65]](#endnote-65)

Addressing the media, Ron Bailey, senior vice-president of Canadian operations, said, “I’m getting kind of the sense that people think that we’re being pushed to do unsafe things and . . . I just want to give a little bit of a personal view on that. I actually believe that CNOOC, by taking us over, has increased our focus on safety. Right from the bottom of their heart, I can say that.”[[66]](#endnote-66)

On July 17, the Alberta Energy Regulator (AER) issued an environmental protection order to Nexen to contain the spill, test for hydrocarbons and chlorides in the affected area, and develop a remediation plan to reclaim the natural environment. Alberta’s chief energy authority said the spill posed no immediate risk to humans or wildlife and had not leaked into any bodies of water.[[67]](#endnote-67)

In a new incident, on August 31, 2015, the AER ordered Nexen to shut down 95 pipelines in Alberta because pipeline maintenance and monitoring were non-compliant. The new provincial government elected in spring 2015 emphasized its intention to hold the oil industry accountable for its environmental impact. Thus, the new minister of energy, Marg McCuaig-Boyd (NDP), said, “The suspension of the pipeline activity won’t be lifted until the company can fully demonstrate that it can operate safely.”[[68]](#endnote-68) Nexen had to shut down about 9,000 b/d of crude production at its facility at Long Lake until the investigation was completed and the pipeline was repaired.[[69]](#endnote-69) By September 17, Nexen resumed full production (50,000 b/d) after AER amended its pipeline suspension order.[[70]](#endnote-70)

On January 15, 2016, an explosion occurred in a hydrocracker facility, which converted tarry oil sands crude into easier-to-refine light oil at Long Lake. One worker died at the site and another seriously injured worker was flown to Edmonton to the burn unit of the University of Alberta Hospital.[[71]](#endnote-71) The plant was immediately shut down, and the SAGD facility was set to minimum production rates. A comprehensive investigation was launched by both AER and the Alberta Occupational Health and Safety organization.[[72]](#endnote-72) The lost production was estimated to be close to 50,000 b/d.[[73]](#endnote-73)

Handling Public Scrutiny

Ever since its bid to acquire Nexen in 2012, CNOOC had faced intensive attention by Canadian stakeholders, who operated quite differently from what CNOOC was used to in China. The leadership team of CNOOC-owned Nexen was especially under pressure to engage with a variety of Canadian politicians, non-governmental organizations, and the media. Following the latest crisis, the top management had to reassess its strategy and practices of engagement in Canada. Had the handling of recent incidents been appropriate, or should its communication strategy be changed?

At the same time, questions arose about whether CNOOC’s international growth strategy itself needed to be adjusted. How could CNOOC change its operational processes to ensure that its health and safety record did not attract unfavourable media coverage? Should CNOOC cut its losses and downscale its engagement in Canada and the oil sands industry in particular? Or, should CNOOC refocus its Canadian operations to use its Canadian assets in a different way?

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Exhibit 1: CNOOC Group Organizational Structure

**The State-Owned Assets Supervision and Administration Commission (SASAC) of the State Council of the People’s Republic of China**

100%

**China National Offshore Oil Corporation (CNOOC)**

100%

50.53%

Indirect holding

59.41%

51.36%

**Shandong Haihua Group Co., Ltd.**

**Offshore Oil Engineering Co., Ltd.**

**Overseas Oil & Gas Corporation, Ltd.**

**China Oilfield Services Limited**

**China BlueChemical Ltd.**

100%

**CNOOC (BVI) Limited**

64.44%

**CNOOC Ltd.**

100%

100%

100%

100%

**China Offshore Oil (Singapore) International Pte Ltd.**

**CNOOC International Ltd.**

**CNOOC China Ltd.**

CNOOC Deepwater Development Ltd.

100%

CNOOC Uganda Ltd.

100%

100%

OOGC America LLC

CNOOC Southeast Asia Ltd.

100%

100%

Nexen Energy ULC

CNOOC SES Ltd.

100%

100%

Nexen Petroleum U.K. Ltd.

CNOOC Muturi Ltd.

100%

100%

Nexen Petroleum Nigeria Ltd.

CNOOC NWS Private Ltd.

100%

100%

Nexen Petroleum Offshore U.S.A. lnc.

CNOOC Iraq Ltd.

100%

100%

Nexen Oil Sands Partnership

CNOOC Canada Energy Ltd.

100%

100%

CNOOC Exploration & Production Nigeria Ltd.

CNOOC Petroleum BRASO Ltd.

Source: CNOOC, 2015 Annual Report, accessed August 13, 2016, www.cnooc.com.cn/attach/0/1606121709183861352.pdf.

Exhibit 2: CNoOC Financial Data—2012 to 2015

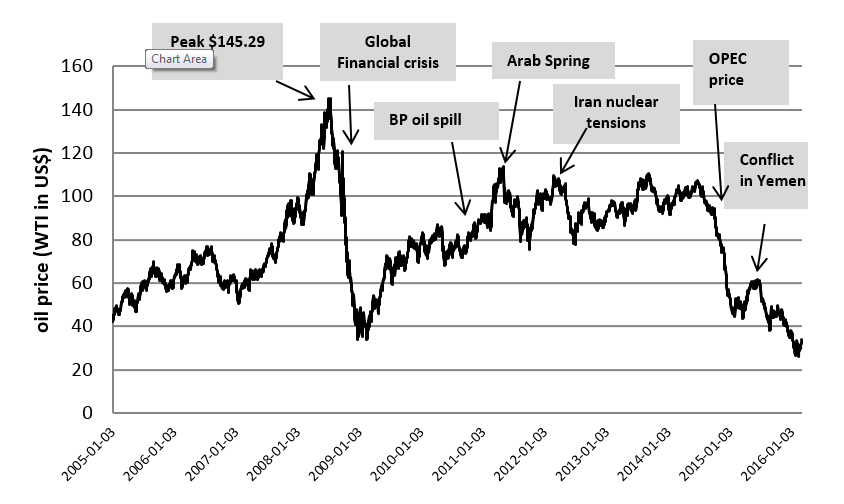
(in ¥ million unless otherwise indicated)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | **2012** | **2013** | | **2014** | | **2015** | |
| **Total** | ***Canada*** | **Total** | ***Canada*** | **Total** | ***Canada*** | **Total** |
| Net sales to customers | 194,774 | *8,800* | 226,445 | *10,555* | 218,210 | *4,981* | 146,597 |
| Total revenue | 247,627 |  | 285,857 |  | 274,634 |  | 171,437 |
| Operating expenses | -21,445 | *-5,794* | -30,014 | *-6177* | -31,180 | *-4,278* | -28,372 |
| Exploration expenses | -9,043 | *-112* | -17,120 | *-1,263* | -11,680 | *-712* | -9,973 |
| Depreciation, depletion, and amortization | -32,903 | *-3,327* | -55,512 | *-6,476* | -57,407 | *-3,163* | -72,665 |
| Finance costs | -1,603 |  | -3,457 |  | -4,774 |  | -6,118 |
| Result of operation | 62,715 | *-722* | 56,160 | *-803* | 62,659 | *-2,136* | 21,315 |
| EBIT | 90,172 |  | 80,851 |  | 82,513 |  | 17,130 |
| EBIT margin (%) | 36.41 |  | 28.28 |  | 30.04 |  | 9.99 |
| Employees (count) | 10,063 |  | 17,553 |  | 21,046 |  | 20,585 |
| Net production  (BOE/day) | 935,615 | *57,534* | 1,127,967 | *67,770* | 1,184,977 | *58,115* | 1,358,022 |
| Net proven reserves  (million BOE) | 3,203 | *803* | 4,139 | *820* | 4,185 | *835* | 4,016 |

Note: EBIT = Earnings before interest and taxes.

Source: CNOOC, 2012 Annual Report, www.cnooc.com.cn/data/upload/2012nianbao.pdf; CNOOC Limited, 2013 Annual Report, www.cnoocltd.com/upload/Attach/mrfj/2014/04/2395984295.pdf; CNOOC Limited, 2014 Annual Report, www.cnoocltd.com/attach/0/1504090826531711217.PDF; China National Offshore Oil Corp., 2015 Annual Report, www.cnooc.com.cn/attach/0/1606121709183861352.pdf; all accessed July 5, 2016.

Exhibit 3: Crude Oil Prices—January 2005 to January 2016



Source: Wind Info, “Futures Settlement Price (Continuous) WTI Crude Oil,” Wind Financial Terminal, accessed June 5, 2016.

Exhibit 4: CNOOC News Release (Excerpts)

**Nexen Energy ULC announces organizational changes in response to industry downturn**

Calgary, Alberta (March 17, 2015)—Nexen Energy ULC (Nexen), a wholly owned subsidiary of CNOOC Limited, has announced organizational changes that will reduce its North American workforce by approximately 340 employees. Nexen UK has also initiated a consultation process to adjust its staffing levels by approximately 60 employees.

“In response to the recent industry downturn that has affected all companies in the energy sector, a decision was made to conduct a thorough review of our organization to ensure our long-term viability and sustainability,” said Fang Zhi, Chief Executive Officer of Nexen. “While regrettable, these organizational changes are necessary to align the company with our reduced capital spending program. We take these decisions seriously, and all impacted employees have been treated fairly and with respect.”

Nexen remains committed to the health and safety of its employees, contractors, the environment and the communities where it operates. The company is fully compliant with all of its Investment Canada undertakings.

Source: “News Release: Nexen Energy ULC Announces Organizational Changes in Response to Industry Downturn,” Nexen, March 17, 2015, accessed August 31, 2016, www.nexencnoocltd.com/en/AboutUs/MediaCentre/NewsReleases/ News/Release.aspx?year=2015&release\_id=AC2705939F6446F692F4AE7F690DD5EF.

ENDNOTES

All websites accessed December 1, 2016, unless otherwise indicated.

1. This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of the China National Offshore Oil Corporation or any of its employees. [↑](#endnote-ref-1)
2. Currency amounts are in US$ or ¥. ¥ = RMB = Chinese renminbi. The exchange rates of the RMB to the U.S. dollar were as follows: 0.15712 as of December 31, 2011; 0.15833 as of December 31, 2012; 0.16356 as of December 31, 2013; 0.16251 as of December 31, 2014; and 0.15407 as of December 31, 2015. The end rates for original sources in Canadian dollars (CA$) have been converted to US$ using the following year-end rates: 1.00312 for 2012; 0.93485 for 2013; 0.85993 for 2014; and 0.72120 for 2015. [↑](#endnote-ref-2)
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