



Local Content Policy Trade-Offs

15th – 17th May 2019

Scenario	20%	30%	40%	50%	60%	70%
Local Content Policy (LCP) - 20%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 30%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 40%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 50%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 60%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 70%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 80%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 90%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 100%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 110%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 120%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 130%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 140%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 150%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 160%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 170%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 180%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 190%	1.00	1.00	1.00	1.00	1.00	1.00
Local Content Policy (LCP) - 200%	1.00	1.00	1.00	1.00	1.00	1.00

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PAGE # 1

Day 1 Program

DAY 1	Local Content Policy, Regulation and Plans
9:00 – 9:15am	Welcome and Course Objectives
9:15 – 9:45am	Definitions and Core Concepts
9:45 – 10:00am	Exercise #1: Local Content Definitions
10:00 – 10:45am	Local Content Policy and Regulations
10:45 – 11:00am	Coffee Break
11:15 – 12:45pm	Exercise #2: Stakeholder Dialogue on Local Content Regulations
12:45 – 1:30pm	Lunch
1:30 – 2:15pm	Local Content Policy Trade-Offs
2:15 – 3:45pm	Exercise #3: Local Content Policy Trade-Off – Modeling Case-Study
3:45 – 4:00pm	Coffee Break
4:00 – 5:30pm	Local Content Plans

Local Content: Trade off between Competitiveness vs Protectionism

DAI Local Content Masterclass - Course Map

DAY 1 Local Content Policy, Regulation and Plans

Definitions

Policy and
RegulationStakeholder
DialoguePolicy Trade-
offsLocal Content
Plans

DAY 2 Local Content Forecasts and Procurement

Industrial Baseline
StudiesLocal Content
ForecastingContracting
StrategyMajor Contract
Tendering

DAY 3 Local Supplier Development and Local Content Reporting

Registration and
Pre-QualificationWriting a
Winning BidLocal Supplier
Development and EDCsReporting and
Metrics

Local Content Regulations Under Pressure



INTERNATIONAL TRADE POLICY CENTER

Local Content Requirements: Backdoor Protectionism Spreading Under the Radar

Contributor: Peter D. Jacobson, PIIE Senior Fellow and Senior Director, PIIE
Date: 10/18/2018, 10:00 AM

“Empirical analyses have shown that LCRs can come at high cost through distorting trade flows, increasing the costs of domestic production, and transferring higher prices to consumers”

WTO Rules for Goods

- **GATT Article III:4** on **National Treatment** provides that imported foreign goods “*shall be accorded treatment no less favourable than that accorded to like products of national origin*”, whether specified in terms of:
 - Particular products
 - Volume or value of products
 - Proportion of volume or value of its local production
- Concept of **national origin** (or **goods of domestic origin**) is based on principle of *substantial transformation*, commonly 40% value-added, but can be lower
 - Preferences based on <40% national origin are still **inconsistent** with GATT Art. III.4 because they break principle of foreign goods being “*accorded less favourable treatment*” than local
- GATT TRIMS Agreement provides ‘*Illustrative List*’ of prohibited preferences, which includes cases where Government mandates **Tender Procedures** for private sector that gives “*advantage*” to domestic origin goods



Information in this slide is not a legal opinion. Please seek own legal advice.

WTO Rules for Services



Workforce

- WTO does **not** specifically preclude governments from mandating national manpower requirements, eg setting quotas or targets for the number nationals in a company or contract sector, either in aggregate or by job position.



Services

- Whether **domestic preferences** for local services are inconsistent with WTO or not, requires investigation of the specific **schedules** under GATS negotiated by the member
 - Schedules are lists of those sectors that the Government opt-in to principles of National Treatment for services



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Important Exceptions to WTO Principles



GATT Art. III.4 does **not apply to ownership** of a good, or ownership of the company manufacturing goods, since ownership is **not** a criteria for determining national origin (eg Angola, Nigeria, Indonesia).

- GPA corrects this anomaly: Article III: "...not treat a locally-established supplier less favourably ..on the basis of degree of foreign affiliation or ownership"



Special and Differential Treatment (SDT) for developing countries no longer apply due to elapsed periods of transition



Private company (eg ICO or foreign contractor) can **voluntarily** preference goods and services of domestic origin (GATT Article III:4 Article only applies to what states/governments can/cannot do to mandate private sector. Hence....



State-owned company (eg NOC or affiliate) cannot preference goods and services of domestic origin because this would constitute a **government obligation in a commercial market**:

- Unless procurement is for **government purposes**, eg public infrastructure (except if signatory to WTO Government Procurement Agreement – GPA)
- ...So key problem is when NOC is in JV with IOC



Information in this slide is not a legal opinion. Please seek own legal advice.

Core Principles of WTO



Under GATTs, government mandated preferences for **goods** of domestic origin are **prohibited-unless-permitted**.



Under GATS government mandated preferences for local **services** are **permitted-unless-prohibited**.



BUT

'In the WTO we are all sinners – everyone violates the rules, all the time. The basic principle is that unless a government is challenged by another member, the regulation is assumed to be consistent with WTO rules'.



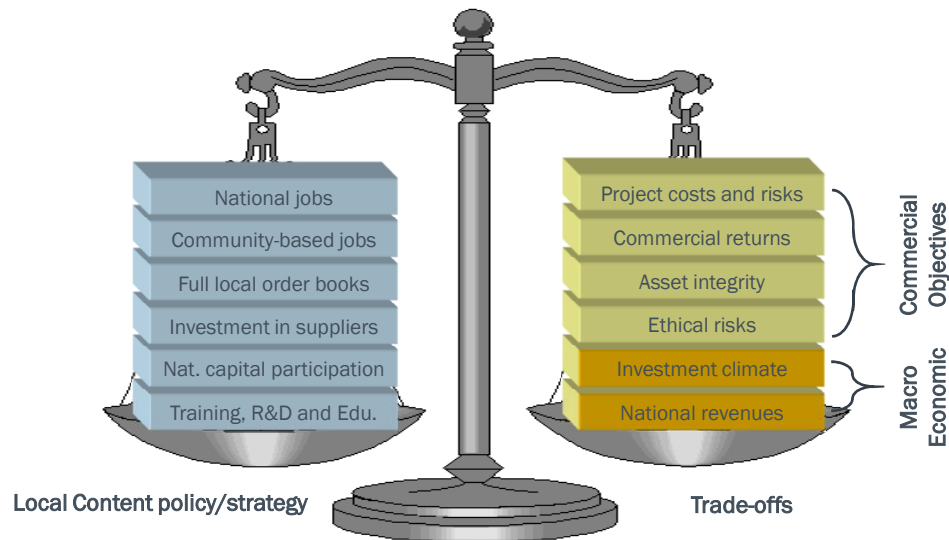
Information in this slide is not a legal opinion. Please seek own legal advice.

Which LC Regulations are Competitive vs Protectionist?

		Competitive based provisions							Risk of protectionism						
	No LC Regulation , Contract terms only	LC Law and/or Regulation and contract terms	Penalties for non-compliance with Law and/or Regulation	First Consideration when competitive	Full and Fair opportunity for local suppliers	Targets agreed, not Govt mandated	Targets within market capability	LCP required, no Govt approval	Notification of tenders, not stages nor Govt approvals	Targets mandated by Govt	Targets risk being beyond market capability	Tender award based in part on LC criteria	Notification of tender stages, and Govt approvals	LCP required, with Govt approval	Market access preference for local ownership or JVs
Protectionist	Nigerian (NOGICD) Act, 2010														
	Ghana L.I.2204/2013														
	Angola Decree 127/2003														
	Tanzania Local Content Regulation 2017														
	Mexico Hydrocarbons Act 204														
	Mozambique Decree Law No.2/2014														
	Sierra Leone Local Content Act, 2016														
Competitive	Canada atlantic Accord Act 1988														
	Oman ICV (PDO) 2014+														
	Guyana (DAI draft policy)														

[illegible]

What does *Optimum* Local Content Look Like?



Exercise # 3

Local Content Policy Trade-Off Modelling

> A \$3 billion **Phase II** remote site development project

- 18 months until investment decision
- New local content public policy under consideration
- What might an *optimal* Local Content policy look like?



Exercise # 3

The Project Scenario

- > **Sub-surface** natural resource development
- > Located **on-shore** in remote coastal province of emerging economy
- > Good **road and rail links** to the concession area
- > **Two towns**: one 20 km from concession with 50,000 inhabitants, the other 40km with 300,000
- > The larger town located on coast with **mature port facilities**
- > Established **local supplier industry** in both towns, with ten years experience in providing goods services to the Phase I project and a similar sized and configured natural resource investment 100km further inland



Exercise # 3

The Project Scenario

> **Phase I Project** (10 years into operations):

- Local content targets set **within capacity of local suppliers**
- CAPEX Phase I: **20%** Local Content
 - Measured as Actual Value Contributed to economy (AVC), ie domestic origin value for goods/equipment, and national labour value for services
- OPEX Phase 1: **40%** Local Content by year 5, steady thereafter
- Tender procedures preference local supplier only if **internationally competitive** on price, quality and delivery



Exercise # 3

The Project Scenario

> Phase II Project under consideration:



- **US\$3 billion** investment
- 10% stake by a state-owned company
- Project Concept in process of being finalised
- **18 months** to final investment decision (FID)
- **Project development** over five years, comprising:
 - In-house project management and engineering design
 - Sub-surface drilling and excavation
 - Construction of on-site primary processing and ancillary facilities
 - Construction of transportation infrastructure to local port for further processing

Exercise # 3

The Project Scenario

> General Principles for Local Content in Phase II have been agreed through a prior process of stakeholder consultation, as follow:

- From 20% to **35%** Local Content in capital expenditure
- From 40% to **50%** Local Content in operational exp., within five years
- Maximise direct and indirect **sustainable employment**, with transferable skills.
- **Unbundled** major contracts to allow for direct procurement to local suppliers
- **New capital investments** in local supply chains – private and public
- **Presumption is to preference indigenous suppliers**, but only if:
 - (i) avoid critical risks, eg no schedule delays
 - (ii) focus on high potential indigenous suppliers offering competitive import substitution
 - (iii) generate long-term cost reductions
- Minimum **11.0% IRR**. 10.0% to 11.0% IRR triggers compensation
- Max Government income forgone for cost recovery for additional Local Content is **\$90 million**

See Handout 1.3



Exercise # 3

The Political Scenario

> Government is proposing a **Job Creation and Industrial Competitiveness** policy

- More Local Content 'now' as a political imperative
- 'Stretch' participation of national labour and local suppliers so that project investment builds local capability for import substitution and export potential in the future



Exercise #3

Local Content Optimisation Modelling - TASKS

Phase II - Scenario #1 – Base Case (same as Phase 1)

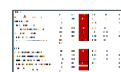
- Local content targets continue to be **within capacity of local suppliers**
- CAPEX Phase I target – remains at **20%** Local Content
- OPEX target – remains at **40%** Local Content
- Tender procedures preference local supplier only if **internationally competitive** on price, quality and delivery

Phase II - Scenario #2 – Optimised Local Content (determined by YOU!)

TASKS

- **Optimise the levels of Local Content** within Phase II, in accordance with the agreed General Principles (previous slide)
- **Populate the Results table**
- **Keep a record** of the rationale for your choice of targets and spend segments

Handout 1.3



Exercise #3

Local Content Policy Trade-Off Module



Cost Estimates
(as % of total)

Current Local
Content targets
(Base Case)

Optimisation
Cells

Max LC with On-
The-Job Training
and Supervision

Max LC with Upfront
Capital Investment,
with Schedule Delay

Total CAPEX	5.0%	11.0%	25.0%	25.0%	50.0%	0
Project - Project Management and Pre-FEED (in-house)	10.0%	2.0%	5.0%	5.0%	15.0%	0
Project - Long-lead items	30.0%	12.0%	25.0%	20.0%	40.0%	12
Project - EPCm Module Fabrication	35.0%	30.0%	55.0%	50.0%	70.0%	12
Project - EPC for Site Construction and installation	11.0%	5.0%	7.0%	7.0%	15.0%	0
Project - EPIC Sub-Surface Engineering	5.0%	60.0%	80.0%	70.0%	80.0%	12
Project - directly contracted services	4.0%	35.0%	45.0%	45.0%	60.0%	0
Project - direct purchase/lease of equipment and materials	100%					
Total OPEX	5.0%	25.0%	30.0%	30.0%	40.0%	0
Operations - In-house professional employees	18.0%	80.0%	90.0%	90.0%	100.0%	0
Operations - In-house non-professional employees	23.0%	70.0%	95.0%	80.0%	95.0%	0
Operations - services contracts (over operational life)	28.0%	20.0%	25.0%	25.0%	30.0%	0
Operations - bulk commodities/materials/routine equipment (over operational life)	26.0%	10.0%	15.0%	15.0%	20.0%	0
Operations - exotic equipment/materials (over operational life)	100%					

Exercise #3

Local Content Model – Main Modules



Economic and Commercial Assumptions

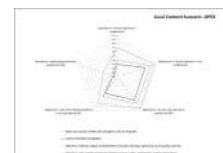
Parameter	Value	Unit	Comment
Project - Project Management and Pre-FEED (in-house)	10.0%	% of total	
Project - Long-lead items	30.0%	% of total	
Project - EPCm Module Fabrication	35.0%	% of total	
Project - EPC for Site Construction and installation	11.0%	% of total	
Project - EPIC Sub-Surface Engineering	5.0%	% of total	
Project - directly contracted services	4.0%	% of total	
Project - direct purchase/lease of equipment and materials	100%	% of total	

Parameter	Value	Unit	Comment
Project - Project Management and Pre-FEED (in-house)	10.0%	% of total	
Project - Long-lead items	30.0%	% of total	
Project - EPCm Module Fabrication	35.0%	% of total	
Project - EPC for Site Construction and installation	11.0%	% of total	
Project - EPIC Sub-Surface Engineering	5.0%	% of total	
Project - directly contracted services	4.0%	% of total	
Project - direct purchase/lease of equipment and materials	100%	% of total	

Local Content Optimisation Module



Local Content
Scenarios
CAPEX and OPEX



Exercise #3

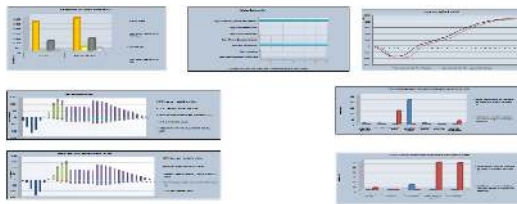
Local Content Model – Main Modules *continued*



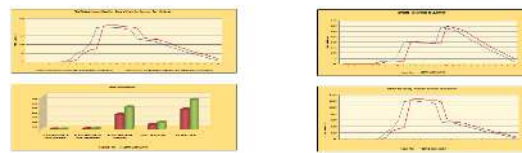
Results Table

Local Content				Impact on Suppliers				Commercial Interests				Government Revenue				Employment Impact				Supplier Impact				Local Supplier Competitiveness Impact			
Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)	Local Content Target (20 years)
64.0%	19.8%	40.0%	34.0%	11,000,000	\$0	\$0	\$0	0	14.5%	44,946,990,943	3.50%	2022	\$1,190,000,000	\$0	\$1,190,000,000	2020	\$9	2,700	23,175	38,900	45,514	\$1,760,000,000	\$0	\$0	\$0	\$0	
64.0%	19.8%	40.0%	34.0%	33,000,000,000	\$0	\$0	\$0	0	14.5%	44,946,990,943	3.50%	2022	\$21,590,000,000	\$0	\$21,590,000,000	2020	\$9	2,700	23,175	38,900	45,514	\$2,760,000,000	\$0	\$0	\$0	\$0	

Results – Commercial Interests



Results – Public Policy Interests



Exercise #3: Results Table

Group	LC% CAPEX (target 35%)	LC% OPEX (target 50%)	Total CAPEX cost (\$billion)	Max Schedule delay (months)	IRR (10.0% min)	National Income foregone (\$MM)	Year of peak National Revenue	Total FTE Jobs created (person-years)	Investment in on-the-job training and supervision (\$MM)	Upfront capital investment in suppliers (\$MM)
Base Case	19.8%	40.0%	\$3.00	0	14.5%	0	2020	64,834	0	0
Max LC with on-the-job training and supervision	31.3% ↑	47.0% ↑	\$3.05 ↓	0	12.3% ↓	\$51 ↓	2020 ↓	82,282 ↑	\$138 ↑	0
Max LC with upfront investment	48.6% ↑	55.5% ↑	\$3.12 ↓	24 ↓	7.0% STOP	\$160 ↓	2022 ↓	105,484 ↑	0	\$363 ↑
Group A										
Group B										
Group C										
Group D										
Group E										
Group F										

Exercise #3: Tasks

Phase II - Scenario #1 – Base Case

- Local content targets continue to be **within capacity of local suppliers**
- CAPEX Phase I target – remains at **20%** Local Content
- OPEX target – remains at **40%** Local Content
- Tender procedures preference local supplier only if **internationally competitive** on price, quality and delivery

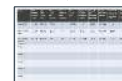
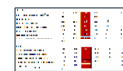
Phase II - Scenario #2 – Optimised Local Content

TASKS

1. **Optimise the levels of Local Content** within Phase II, in accordance with the agreed General Principles (**red cells ONLY**)
2. **Populate the Results table** (*start by validating first 3 rows in Results Table to understanding the Local Content limits of each category*)
3. **Report your results to Trainer** (**green cells**)
4. **Keep a record** of the rationale for your choice of targets



Handout 1.3



Debrief

Exercise #3: Results Table

Group	LC% CAPEX (target 35%)	LC% OPEX (target 50%)	Total CAPEX cost (\$billion)	Max Schedule delay (months)	IRR (10.0% min)	National Income foregone (\$MM)	Year of peak National Revenue	Total FTE jobs created (person years)	Investment in on-the-job training and supervision (\$MM)	Upfront capital investment in suppliers (\$MM)
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Max LC with upfront investment	48.6%	55.5%	\$3.12	24	7.0%	\$160	2022	105,484	0	\$363
Group A										
Group B										
Group C										
Group D										
Group E										
Group F										
Group G										
Group H										

Debrief

- Quantification of economic impacts of Local Content policy and strategy, even if only indicative, can inform a rationale stakeholder **dialogue** and help **forecast** the economic and commercial impacts
- Different expenditure categories exhibit **different sensitivities** to Local Content, eg with regard to cost, jobs, IRR, national income etc.
- Some expenditure categories may present **too high a risk/cost** to be the focus of Local Content development, eg schedule delay
- Other categories may be **'stretched' on-the-job**, but at a \$ premium, up until a threshold is reached when **upfront capital investment** is needed, which then may (or may not) cause schedule delay
- The period from FEED up to FID is an opportunity for upfront investment
- Some of the fundamental **trade-offs** include:
 - IRR vs Local Content %
 - Project cost vs # jobs
 - Local Content % vs national income

LOCAL CONTENT OPTIMIZATION RESULTS

Scenario	LC% CAPEX	LC% OPEX	Total CAPEX (\$B)	Max Delay (mo)	IRR (%)	Nat Income (\$MM)	Peak Rev Year	FTE Jobs	On-Job Training (\$MM)	Upfront Capex (\$MM)
Base Case	19.8%	40.0%	3.00	0	14.5%	0	2020	64,834	0	0
Max LC with on-the-job training and supervision	31.3%	47.0%	3.05	0	12.3%	51	2020	82,282	138	0
Max LC with upfront investment	48.6%	55.5%	3.12	24	7.0%	160	2022	105,484	0	363
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