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SUBJECT: RRT ERBIL: CONSORTIUM TO DEVELOP GAS FIELD IN
KURDISTAN REGION TO FEED NABUCCO PIPELINE

¶1. (SBU) Summary: UAE's Crescent Petroleum and Dana Gas have entered into a consortium with two European energy companies to develop a natural gas field in the Kurdistan Region (KR) to supply the Nabucco pipeline. Separately, Crescent/Dana's plans to develop Gas City, a massive gas utilization industrial complex, in Sulaimaniyah Province are in limbo due to foot dragging by the Kurdistan Regional Government (KRG). Meanwhile, Crescent and Dana are looking to build gas cities in Anbar and Basra provinces, although progress on these is being held up by what they describe as central government "blackballing" of energy companies with stakes in the KR. KRG Minister of Natural Resources informed RRT Team Leader that the KRG was not in negotiation with Crescent/Dana, stating "if and when gas becomes available, then the KRG or Iraq will need to come up with a commercial arrangement for selling/pricing the gas - which belongs to all the Iraqi people." End Summary.

¶2. (SBU) On May 17, Crescent Petroleum and Dana announced that they had entered a consortium with two European petroleum companies to supply gas to the Nabucco pipeline from fields in the KR. The Nabucco pipeline will pump natural gas to Austria via Turkey from several possible sources, including Azerbaijan and Iran, thus reducing the dependence of European countries on natural gas from Russia. It is expected to be completed by 2014.

The Consortium

¶3. (SBU) Crescent Petroleum, based in the United Arab Emirates, is the first and largest privately-owned natural gas company in the Middle East, according to Shakir Shakir, Kurdistan Branch Manager for Dana Gas. The company is led by a Cambridge University-educated Iraqi exile, Hamid Jafar, whose father had been Minister of Development in the cabinet of Iraq's last king. In 2005, Crescent established Dana Gas as a publicly-traded natural gas company. Although Crescent owns a controlling share of Dana (21 percent), Dana has over 300,000 shareholders in over 100 countries. The two companies established a local subsidiary, Pearl Petroleum, to handle their upstream interests in the KR.

¶4. (SBU) The two European companies joining Crescent/Dana are OMV of Austria and MOL, the Hungarian Oil and Gas Company. Both companies are shareholders in the company developing the Nabucco pipeline. Under the agreement with Crescent/Dana, OMV will purchase a 10% interest in Pearl for \$350 million, which will be reinvested in the project. In exchange for giving MOL a 10% interest in Pearl, Crescent and Dana will receive a 3% share in MOL. (Note: The director of London-based think tank Iraq Energy, who has close ties to Crescent Petroleum, said the value of the stock swap was also roughly equivalent to \$350 million. End note.) This gives Crescent/Dana an indirect interest in the Nabucco pipeline project as well as in MOL's operations in the KR.

Chamchamal Natural Gas Field

¶5. (SBU) All the natural gas that the Crescent/Dana consortium plans to supply to the Nabucco pipeline will come from the Chamchamal natural gas field, which is still under development. None of the natural gas from Chamchamal will be needed to feed the KR's two BBO power plants in Pir Daoud and Chamchamal power plants. The entire demand for natural gas for these two power plants will be fully met by Crescent/Dana's natural gas field in Khor Mor, where

QCrescent/Dana's natural gas field in Khor Mor, where Crescent/Dana are expanding production with the drilling of a ninth well. Both fields are in Sulaimaniyah Province.

(Note: Chamchamal's production reserves are estimated to be 2.2 trillion cubic feet, tcf. The USAID Economic Development Assessment, however, states that the total potential reserves of both fields are 11.7 tcf, and Chamchamal is the larger of the two fields. End note.)

Technical Challenges Surmountable

¶6. (SBU) The consortium will need to build a pipeline to tie the Chamchamal field with the Nabucco pipeline. The mountainous terrain between the two points will present technical challenges. The consortium, however, is confident that it will be able to surmount them without problems, according to Shakir. These challenges, he continued, are less daunting than those that Crescent/Dana faced when building the existing 180 km pipeline between the Khor Mor natural gas field and the electrical power plants in Chamchamal and Pir Daoud. That pipeline not only had to pass through rugged terrain, but through minefields, as well.

Political Risks Acceptable

¶7. (SBU) All parties in the consortium have studied the political risks they face, and are confident that these will not impede the project's success, Shakir asserted. All of the companies did due diligence, and the three publicly listed companies are answerable to stockholders, adding to the cautious approach they took. The first consideration was the GoI. According to Shakir, lawyers assured the consortium that the Iraqi constitution and all relevant laws supported their venture, even though the GoI has already expressed its disapproval. Shakir discounted a press report quoting Iraqi government spokesman Ali Dabbagh, who said that the

consortium's deal to export gas to the Nabucco pipeline was illegal. Not only does the law favor the consortium, Shakir said, quoting the findings of the consortium's lawyers, but the fact that the GoI recently allowed oil to flow to the strategic pipeline from Tawke and Taq Taq shows that the government, in the end, is responsive to the need for higher export revenues and the facts on the ground.

¶8. (SBU) The consortium must deal delicately with the issue of Iran for two reasons, according to Shakir. First, Iran itself is a competitive source of natural gas. Second, the success of the consortium in the KRG would strengthen Iraq at the expense of Iran; and Iran wants a weak Iraq. Russia, also, stands to lose ground if the Nabucco pipeline succeeds.

On the other hand, Turkey is delighted with the prospect of receiving gas from Kurdistan, according to Shakir. The success of the Nabucco pipeline is very much in Turkey's strategic interest, he observed. The more possible sources of natural gas, the greater the advantage to Turkey.

¶9. (SBU) Comment: OMV and MOL are already exploring for oil in the KR under production sharing agreements (PSAs), so both OMV and MOL already have an exposure in the KR that might have led them to conclude "in for a penny, in for a pound." OMV signed a PSC in November 2007 to develop two exploration blocks, while an MOL subsidiary partnered the same month with a UK Gulf Keystone subsidiary to develop another block. End comment.

Other Crescent/Dana Projects inside Iraq

¶10. (SBU) Crescent Dana is negotiating with the United Cement Company to provide natural gas from the Khor Mor field to cement factories at Bazian and Tasluja, both located in Sulaimaniyah Province. United Cement's major shareholder is the French building materials giant, Lafarge. Currently,

these factories rely on fuel oil trucked from the Bayji refinery. Natural gas, besides being environmentally cleaner, will be a much cheaper source of energy. Lower energy costs should enable United Cement to compete more effectively against cement imported from Iran, which currently undercuts the locally produced product (reftel).

¶11. (SBU) Meanwhile, Crescent/Dana's ambitious plans to build Kurdistan Gas City, a gas utilization industrial complex near Chamchamal, remain on hold. As envisioned, the project would cover 43 square miles, an area larger than the size of the city of Sulaimaniyah, and create up to 200,000 jobs in the Qcity of Sulaimaniyah, and create up to 200,000 jobs in the region. The project will require active coordination by several ministries, as well as the participation of many investors. But so far, Shakir said, the KRG has not focused on it, and has not even allocated any land.

¶12. (SBU) On the other hand, Crescent/Dana has been actively studying plans to build a gas city in Anbar Province, using natural gas from the Akkas gas field. According to Shakir, Anbar tribal chief Sheikh Ahmed Abu Risha enthusiastically supports the idea. Sheikh Ahmed told Crescent/Dana he welcomes the jobs that the project would create, adding that right now the only possibilities open to young men in Anbar are either to join the police or Al Qaeda. Shakir also mentioned plans to build another gas city in Basra Province. The problem with proceeding forward with either of these plans, Shakir explained, is that Oil Minister Shahrastani has blackballed hydrocarbon companies doing business with the KRG from doing business in the rest of Iraq.

Comment

¶13. (SBU) This announcement was made by consortium itself, and not by the KRG. But this project fits in well with the KRG's strategy to develop its hydrocarbon resources at all

deliberate speed, consistent with regional legislation passed in 2007. KRG Minister for Natural Resources Ashti Hawrami told the RRT Team Leader that the KRG supported the idea although it was not negotiating with the consortium at this time. "If and when gas becomes available, then the KRG or Iraq will need to come up with a commercial arrangement for selling/pricing the gas - which belongs to all the Iraqi people," he stated.