Prospects for Kenya's Turkana-Lamu Oil Pipeline

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Overview

The Turkana county in North West Kenya is the poorest of Kenya's 47 counties despite being the second largest by land mass. Hope for improvement of economic prospects in the county have been raised by the predicted 750 million barrels of commercial oil reserves which have been discovered in the Turkana basins. An 865km pipeline is proposed for construction to transport crude oil from the Turkana basins to the port city of Lamu, South West Kenya, at an estimated cost of $USD2.1bn. Lamu was chosen as the port due to its existing oil infrastructure including an oil refinery. Completion of the Turkana-Lamu oil pipeline is expected in 2021.

Fourteen oil exploration prospects have already been drilled and 11 accumulations discovered by Tullow Oil in the South Lokichar basin of Turkana. Tullow Oil owns 50% of the two blocks where discoveries were made in 2012 with Africa Oil and A.P. Moller-Maersk each having a 25% share. Indicative of their commitment to the project, Tullow Oil allocated ~$USD80m of its $USD460m capital operating expenditure in 2018 to pre-development in Kenya.

Impact on the local population

There was an initial expectation that the discovery of oil in Turkana would bring jobs and prosperity to the local population. However, this has not been the case as Tullow Oil has had to hire Kenyan workers from other counties due to a lack of trade skills from the predominantly agricultural population of Turkana. Consequently, there has been a rise in discontent amongst the local population which led to 200 Tullow oil employees being taken hostage by members of the Lokichar community for several hours in January 2018.

Local communities in Turkana are set to benefit from an increased share of profits from oil revenue. This is linked to a proposal endorsed by the government's Energy Committee to raise the share of government revenue from petroleum sales for local communities from 5% to 10%. It is likely that this will prove popular with communities in Turkana who increasingly require financial assistance due to frequent drought.

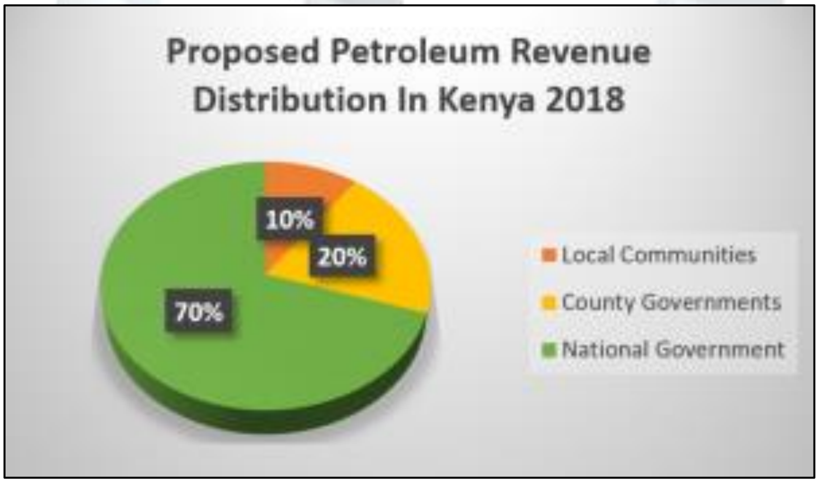

Image 1. Proposed Petroleum Revenue Distribution in Kenya.

Analysis of project development

Tullow Oil has stated that it will produce 2,000 barrels per day (bpd) from the Lokichar oil fields. Until the Turkana-Lamu pipeline is complete, oil will be transported via trucks to the port of Mombasa for shipping to international markets. Meanwhile, development has already begun at Lamu, which is planned to have the largest port in East Africa by 2020. The Kenyan government is still looking to attract foreign investors as the main source of funding for the pipeline which is reported to require oil prices between $USD50-$USD55 per barrel to be profitable. This shows positive signs for attracting investors as Brent crude prices currently sit above $70 per barrel. Efforts to attract investors received a boost in January 2018 when French firm Total SA publicly affirmed its commitment to the project. Total SA have also committed funds to the Uganda-Tanzania crude oil pipeline in a move which may signal a diversification of risk in its East Africa oil portfolio. Involvement of Total SA is likely to give other investors' confidence due to the company's participation in various projects across East Africa which has made it one of the regions key developers of petroleum resources.

Outlook:

- Oil companies operating in Turkana who fail to conduct meaningful stakeholder engagement and Corporate Social Responsibility (CSR) are likely to experience disruption to their operations from local communities. Where companies demonstrate long-term investment in local communities by expanding the prospects of future employment, they are likely to reduce operational disruption. This is becoming increasingly relevant as persistent drought will decrease the amount of farming work available in Turkana over the next 10 years.
- The Uganda-Tanzania pipeline is likely to be the main source of competition in terms of investor finance for the Turkana-Lamu pipeline. It is possible that investors may spread investment across both projects in a similar way to Total SA to diversify their risk.
- Delays in securing funding and investment make it possible that the Turkana-Lamu crude oil pipeline will not be completed by 2021.
- While global oil prices remain above USD$55 the Turkana-Lamu pipeline will be profitable, this will increase the likelihood of attracting required investment.
- Until the pipeline is complete, disruption along Kenya's roads threatens to delay deliveries of oil to Mombasa port which could have impact throughout the entire oil export chain. Despite there being little alternative to relying on trucks for logistics in Kenya, the roads are generally in a state of disrepair and criminality is an ever-present threat. Further compounding these threats to logistics is the possibility of protests and strikes by truck drivers intended to force the government into action.

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