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OILFIELD EQUIPMENT: Pumping up spending to grease the way for petro-profits

By Brian Dunn Published: Mar 1 2008

With all three facets of the energy market-upstream, midstream and downstream-currently thriving, some companies servicing the sector are hoping to reap the rewards by pumping up capital expenditures.

Driven by a combination of strong demand, inadequate production and refining capacity and geopolitical risks, the fundamentals supporting higher oil and gas prices are structural and likely will persist for several years, according to Dresser-Rand Group Inc., Houston, a major supplier of rotating equipment for the oil, gas, petrochemical and industrial process industries.

Natural gas prices peaked at $14.994 per million British thermal units (mmBtu) in December 2005, according to data from the U.S. Energy Information Administration (EIA) based on the settlement for the Henry Hub natural gas spot contract on the New York Mercantile Exchange (Nymex).

While current natural gas prices are about 47 percent below that level, they have been showing relatively small but steady gains since last August. Based on actual working days, *AMM* calculated the natural gas spot price averaged $6.137 per mmBtus in August, rising to $6.189 in September, $7.224 in October and $7.778 in November before easing back to $7.179 in December, but were hovering in the $8-per-mmBtu range in January.

Crude oil futures hit the psychologically important $100-a-barrel level on Nymex on Jan. 2 amid concerns over supply and fears of falling U.S. stock levels. Prices had averaged $72.36 a barrel in August, rising to $79.63 in September, $85.66 in October and $94.63 in November, according to the EIA data. Like natural gas, prices eased back slightly in December to average $91.74 a barrel before entering the new year with a bang.

With prices at these levels, it is no surprise that companies servicing the sector might hope to get in on the action.

In the upstream market, the number of facilities, including floating, production, offloading and storage vessels, is expected to increase significantly during the next five years, while the liquefied natural gas market is expected to double capacity in the next 10 years.

In the midstream segment, nearly 40,000 miles of natural gas pipelines are planned for construction, Dresser-Rand said.

The downstream refining market has been particularly strong in the United States in recent years due to clean-fuel initiatives, the company said. More recently, there has been a significant effort toward boosting refining capacity internationally, propelled by the "mismatch of heavy sour crude conversion and refinery utilization rates, (which) are at their highest levels in 25 years," the company said. "The current industry view is that refining capacity will increase by approximately 11 million barrels per day by 2010."

Canada's largest energy services provider, Precision Drilling Corp., Calgary, Alberta, has earmarked a record $370 million in capital expenditures this year, up 70 percent from 2007. The bulk of the money-$260 million-is slated for the construction of 19 new high-performance "super series" land drilling rigs, which offer higher pumping capacity, more versatility and better mobility than traditional rigs. They are scheduled to be delivered over the next six to 18 months.

About 70 to 80 percent of land drilling activity in North America is for natural gas-a market that's feeling squeezed in Canada but is performing well in the United States, according to Doug J. Strong, Precision Drilling's chief financial officer.

"It's been tough, which is reflected in the drop in drilling activity in Canada. But the U.S. has held up well," he said. "Pricing goes in line with the supply of gas and inventory levels, and U.S. inventory levels have been riding along the five-year highs for close to two years. But they've come off recently, which has provided a bit of optimism in market activity because it's difficult for our customers to replace reserves, so we're feeling positive long term."

With fewer opportunities in Canada, Precision Drilling expects to double the number of rigs it operates south of the border to 24 this year from 12 currently, primarily in Colorado and Texas.

Unlike offshore rigs, which are facing a supply problem, Strong said there's an abundance of land drilling rigs, although not necessarily the high-performance rigs that operate 20 to 40 percent more productively. "There's always opportunity in the high-performance end of the market where we operate, which ultimately lowers well costs, and we still see opportunities in Canada and to diversify outside of Canada."

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