DRILLING CONTRACTOR

DRILLING AHEAD

Rigs, people: You can't always get what you want—only what you need

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THE DISGRUNTLED CALLER didn't understand why the small producing firm he had invested in could not secure a rig for a make-or-break drilling project. "Don't you think," pondered the would-be wildcatter, "that this demonstrates poor planning?"

Well, my friend, welcome to the oil patch!

Such a question is truly breathtaking in its panoramic ignorance of drilling market dynamics. We reap what we sow in rig availability. The same dynamic holds true for people, the other critical shortage we face. In lean times, it would be a foolish contract driller who would speculatively invest millions of dollars on a new land rig, or hundreds of millions for an offshore unit. In publicly traded companies, shareholders would have management's heads on a platter. Owners of private firms would find themselves queuing up at soup kitchens.

Only the operator community has the resources to plan for good times during the bad. But just a handful of operators can afford the luxury of long-range investment when oil prices are low and rig supply wide open. Even for a mega-major, justifying an investment exceeding a quarter of a billion dollars for a newbuild deepwater MODU with oil prices in the mid-teens is a tough sell. Over the long term, though, securing a long-term agreement with a hungry contractor to build a state-of-the-art rig makes economic sense.

Unfortunately, such investment in rigs and people did not come to pass during the long years of drilling depression, and we reap the results today.

The good news is that the market is responding to demand. IADC just completed its annual membership drive, and the results are stunning. The number of IADC contractor members shot up to 329 from 273 in 2005, a 20% increase. The areas of most marked increase are among land contractors based both in the US and in the IADC-defined international region (i.e., outside the US and Europe). In the US, the IADC land-drilling community saw a 25% increase to 176. Internationally, IADC land contractors shot up 32% to 66 companies.

And there are more rigs. The fleet of shallow-drilling land rigs (less than 15,000-ft depth capacity) burgeoned to 2,057, a jaw-dropping 267-rig (15%) increase from '05. These rigs represent the low end of the investment spectrum, so expect more expensive and deeper-drilling rigs to follow. Several individuals with greater mastery of land and offshore drilling economics present their points of view elsewhere in this issue.

The financial drivers underlying rig-fleet growth are significant. The celebrated analyst **James Wicklund** of **Banc of America** observed during the recent IADC European Well Control Conference that this marks the first time in 18 years that the rate of return on building new land rigs has exceeded 18%. In fact, he said, the current return for land-rig construction ranges between 28% and 35%. Small surprise that manufacturing capability is strained to the limit. Mr Wicklund estimates the total cost of the land-rig upgrade at $1.9 billion.

Figures for the offshore segment are even more dramatic, with 72 new marine rigs projected to come on stream by 2010 at a total cost of $14.9 billion. The census of mobile offshore rigs within IADC's membership has already swollen by 8. That's not much in a 542-rig universe, but it is the leading edge of a growing fleet.

The bottom line is that, while our resources of rigs and people may not be optimal for today's go-go E&P business, we are not treading water. To paraphrase a rock-and-roll star now long in the tooth (not unlike many of us in this business), "You don't always get what you want, but if you try real hard, you just might find you get what you need." ■