Sinopec to Bet on Shale for Growth to Offset Refining Losses

By Bloomberg News - Aug 30, 2011

China Petroleum & Chemical Corp. (600028), Asia’s biggest refiner, will collaborate with overseas companies to step up its search for shale gas resources as it seeks to diversify away from unprofitable crude processing.

“Future growth will mainly come from unconventional gas,” Fu Chengyu, chairman of the company known as Sinopec, said in Hong Kong yesterday. “Our technology and experience still lags behind western oil companies, but we don’t have to wait until our technologies mature. We can hire them to work for us.”

Sinopec will join rival PetroChina Co.’s parent and Cnooc Ltd. (883) to seek technology through partnerships as China, estimated to hold more gas trapped in shale than the U.S., opens new areas to exploration. Results of 20 experimental shale-gas wells Sinopec has drilled in China are “better than expected,” and it will increase investments over the next decade, Fu said.

“It’s going to take two to four years before they know how to do shale gas, or to find out if there’s anything useful there,” said Brynjar Eirik Bustnes, a Hong Kong-based analyst at JPMorgan Chase & Co. “Gas itself is so small for Sinopec that the impact on overall business won’t be there for many years. Beyond 2015, shale gas may become a growth driver.”

Chinese shale may hold 1,275 trillion cubic feet of gas, or 12 times the country’s conventional natural gas deposits, the U.S. Energy Information Administration said in April. China’s “technically recoverable” reserves are almost 50 percent more than the 862 trillion cubic feet held by the U.S., the EIA said.

Shares Rise

Sinopec has climbed more than 21 percent in Hong Kong trading in the past year compared with a 2.6 percent drop in the benchmark Hang Seng Index. The stock rose 0.8 percent to HK$7.55 today. It gained 6.7 percent yesterday, the most in 20 months, after the Beijing-based company posted a record first-half profit that beat analyst estimates.

State-controlled Sinopec said on Aug. 28 net income rose 12 percent to 41.17 billion yuan ($6.5 billion) after it minimized refining losses by keeping oil costs in check while increasing fuel output. The refiner’s
12.2 billion yuan loss from turning crude into gasoline and diesel was about half of PetroChina’s even as it processed 62 percent more oil than its rival.

Earnings from refining may improve in the second half after crude fell 12 percent from its peak in April. Analysts expect inflation to ease, allowing the government room to increase domestic fuel prices that have trailed crude costs.

‘Trying to Lose Less’

“We are trying to lose less when everyone is losing money in” refining, Fu said at a media briefing. “When the industry recovers you will see where our core competitiveness lies. We will make more profit than any of our competitors in China.”

Refining and marketing accounted for 58 percent of Sinopec’s revenue in the first half, while exploration and production had a 5.2 percent share.

China National Petroleum Corp., PetroChina’s parent, agreed in June to form a venture with Royal Dutch Shell Plc to improve its drilling efficiency after taking 11 months to complete the country’s first shale well. Baker Hughes Inc., the world’s third-largest oilfield services provider, says it has helped U.S. shale developers to cut drilling time to about 16 days a well.

Overseas explorers, barred from bidding in Chinese auctions of shale areas, are in discussions to forge local ventures. Chevron Corp. and BP Plc are in talks with Sinopec and its parent, China Petrochemical Corp. Norway’s Statoil ASA is in negotiations to buy stakes in shale-gas assets in China.

China currently doesn’t produce any shale gas. Annual shale-gas output in China may reach 20 billion cubic meters (706 billion cubic feet) by 2020, Pan Jiping, a researcher at the land ministry in Beijing, said in June.

Shale-rock formations require injection of water, sand and chemicals to release gas. Environmental groups have opposed using the process called hydraulic fracturing, or fracking.

“In China, unconventional will surpass conventional gas,” Fu said yesterday.

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