Outlook for the Nigerian Energy Sector, 2022

With the year 2021 just behind us, many have considered key issues such as post-covid conditions, economic revival, and better currency stability to be some of the key highlights we can expect to see in this year.

Notably, the year 2022 is the year before the general elections and 'politicking' is expected to be in full swing by Q3. However, quite a lot is still expected to happen in the energy sector this year.

From the Oil & Gas sector to the electric power value chain, to the role to be played by renewable energy, this piece reviews the likely events that will shape the Year 2022, particularly, for Nigeria's energy sector.

The Oil & Gas Sector (Upstream, Midstream and Downstream)

Divestments- Opportunities for Juniors, Indigenous and Independents?

Considering that many oil companies are looking to transition towards cleaner energy, it is expected that lots of the majors are likely to up their stake and investments, as they look to concentrate more on gas and renewables. Interestingly, these companies are already investing more, especially, outside of Nigeria. They are also beginning to name-change from exploration and production companies (purely hydrocarbons companies) to energy companies, in a manner that reflects their growing interest in clean energy sources, and this trend is expected to continue.

Also, industry challenges (especially security issues), with onshore exploration and production will mean divestments and movement deep offshore. With such divestments, it appears that indigenous companies who appear better able to deal with such security issues (utilizing local/indigenous solutions) will make efforts to acquire many of these assets. Consequentially, we are likely to see more juniors and independents buying some of these assets and we are already advising a few in connection to this.

Importantly, Nigeria appears to be losing potential risk capital to countries such as Brazil, Guyana and the Permian Basin. It is certainly a situation that we hope key stakeholders can address and cause the tide of growing investments to sway in our favor.

Natural Gas to be Treated as 'Green' Fuel as the World Seeks to Transition

We predict that natural gas will become increasingly important, despite the clamor for net zero and decarbonization. The well-documented challenges with non-carbon energy sources, especially around technology and financing (huge volumes required in developing countries compared to conventional energy/hydrocarbons) would mean that financing will still be available for gas infrastructural projects, and most countries will continue to use natural gas, and place more emphasis on natural gas than the world had ever done. The advantage to be seen, is that, if well-exploited, Nigeria, with its huge 206 tcf of proven gas reserves, stands to benefit from the increasing global and economic importance of natural gas.

Nigeria is on the right track, by declaring 2021-2030, the decade of gas. Although, much more needs to be done to exploit the country's gas resources and drive economic growth with natural gas. The private sector and existing gas players will continue to push the gas story and achieve growth in the mid and downstream gas segments. We also expect gas projects such as the Ajaokuta-Kaduna-Kano Natural Gas Pipeline project to close and/or make substantial progress this year, to ensure we begin to reap the benefits of the huge investments already made.

It will be needful, for the government to ensure that the flare gas commercialization program is successful, and that flare gas is utilized for value-adding projects and transactions, as projected.

Removal of Subsidy on Petrol (Premium Motor Spirit) and the Dangote Refinery

Generally, the country and its successive governments have appeared to elevate politics above policy, such that any unpopular decision, even when in the best interest of the nation, in the mid to long term, is usually denigrated, especially, when it is perceived to adversely affect the electoral fortunes of the ruling political party or administration. One of those has been the debate around the removal of subsidy. Irrespective of whatever the motivations may be, political signals suggest the likelihood that the government will finally remove subsidy this year, as the current administration is unlikely to make such sensitive decisions in the year of elections, 2023.

To an extent, a positive for the current administration seems to be that fuel queues are a thing of the past. It is also likely that existing government refineries will also be rehabilitated, or at least, the rehabilitation will commence. The Dangote Refinery is likely to commence operations this year, and hopefully, the projections are right that its operations would make the feared effect of subsidy removal on the masses less evident.

The Electric Power Sector (Generation, Transmission and Distribution)

NERC Commissioners Tenure Ends

To Stay or Not to Stay? -The current tenure of the exiting Nigerian Electricity Regulatory Commission (NERC) Commissioners ends in February 2022, and if history is anything to go by, their exit is unlikely to slow down the activities of Commission. Whilst the President has the power to renew the tenure of these commissioners, there is no certainty that this would be the case as the jury is still out on their overall performance.

Marginal Improvement in the Distribution of Power: We expect to see electric power distribution substantially improve in areas where people pay for services and Distribution Companies (DisCos) moving from areas where the end users of electricity do not pay for the power supplied. There is likely to be the adoption of various DisCos Franchising Models (Metering, Billing, and Collection). The NERC Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry 2020 (the Franchising Guidelines) was issued to enable DisCos to take advantage of evolving business structures and technology for the purpose of providing adequate safe and reliable services to end user consumers. The Franchising Guidelines permit a DisCo to enter a franchising arrangement with a third party (Franchisee) which authorizes the Franchisee to perform some of the specific functions of the DisCo within the DisCo's licensed area.

Improvement in Distributed Energy Resources (DERs)

The movement towards integrated grid with efficiency and consumption working together for mutual benefit is advancing rapidly and more of this is expected in 2022. The deployment of more DERs are certainly going to be a big influence on these projections. DERs are small scale unit of power generation/mini grids that operate locally and are connected to a larger power grid at the distribution level. They are also intended to operate independently from the local distribution licensee

In recent years, support for mini-grid development has increased due to improved commercial viability and recognition of the co-benefits of electrification, such as local economic development. By Nigerian electricity law, mini-grids are stand-alone power generation systems of up to 1 MW capacity that provide electricity to multiple consumers through a distribution network. They differ from embedded generation, which are independent power plants connected to the centralised grid at the distribution level. Today's mini-grids demonstrate greater availability, reliability, and customer value compared to current alternatives in most rural areas.

The NERC Mini-grid Regulations, 2016, are designed to promote investments in rural electrification, and provide a framework for engagement between mini-grid developers (off-grid electricity), community stakeholders and existing distribution companies, private retail tariff arrangements for certain operators, and compensation for developers in the event of operational expansion by the distribution company licensed to cover the relevant community.

The available mix of DERs have changed the power generation sector by disrupting traditional markets and models as there is an evolving landscape for solar, wind, battery storage and other new energy technologies in the power space. It has paved and will continue to pave the way for a two-way flow of energy, and allows the incorporation of new, connected technologies for power generation.

The Year of Siemens- Improvement in Power Sector Infrastructure

The challenges of power supply in Nigeria negatively affects the industrial, agricultural, and mining sectors, hindering the development of the nation's economy.

Thus, as part of measures to address the monumental infrastructural gap in the power sector, the Federal Government of Nigeria (FGN) in July 2019, signed an implementation agreement with Siemens AG (**"Siemens"**) for the Nigeria Electrification Roadmap (**"NER"**) in the bid to resolve existing challenges in the power sector, and expand the capacity for Nigeria's future electricity needs. The Nigeria-Siemens electricity programme is for the delivery of about 7,000 megawatts of electricity, and is expected to kick-off fully this year 2022, with consultants (including legal) having already been appointed in this respect.

The NER is designed to be implemented in three (3) phases over the span of six (6) years, from 2020 to 2025. Phase 1 entails an upgrade of the operational capacity of the power sector system to 7GW, which will be followed by measures to address other impediments to the full use of existing generation and distribution capacities, and increase the power sector system operational capacity to 11GW under Phase 2. Furthermore, it is contemplated that upgrades and expansions across the generation, transmission, and distribution segments of the power sector in Phase 3 will lead to an increase in operational capacity to 25GW.

The various projects under the three phases of the NER are to be executed by a consortium of Siemens and its Nigerian subsidiary, pursuant to relevant construction contracts to be executed between the consortium and the Bureau of Public Enterprises (**"BPE"**).

Whilst the various projects cut across the transmission segment (controlled by the FGN through the Transmission Company of Nigeria ("TCN")), as well as the generation segment (controlled by the private sector), and the distribution segment (controlled by the private sector - the BPE holds shares in the distribution companies), it is understood that the BPE will be entering into the construction contracts on behalf of the FGN as well as other stakeholders in the sector. It is expected that this arrangement will improve the overall value chain.

The primary objective of Siemens in the first phase of project implementation will be to increase power delivered to end-use customers by additional 2GW, significantly reduce Aggregate, Technical, Commercial and Collection (**"ATC&C"**) losses and achieve improved grid stability and reliability.

Privatization of the National Integrated Power Projects (NIPP) and some Government Mid/Downstream Energy Assets

The problem with the power sector in Nigeria has not always only been about power generation (including for pass-through such as gas). If the existing transmission and distribution problems are resolved and connected customers pay for the power consumed as at when due, we can expect the generation sector to thrive better.

There is already a lot going on with the off-grid generation segment, and I think the country does need to promote distributed/off-grid generation to meet its power needs in the short to medium term, especially, for residential and commercial consumers, whilst industrial and more heavy users can concentrate on the national grid.

It is expected that the planned sale of the five (5) power plants under the NIPP will close by end of Q3/beginning of Q4, this year, such that the country can also raise some revenue and have the said plants more efficiently run by private sector experts.

Additionally, a number of concession programmes are ongoing with respect to some government-owned energy assets with relevant regulatory and governmental approvals obtained for same. We expect a number of these to close at anytime between Q3 and Q4 this year.

Concluding Remarks

With the passage of the Petroleum Industry Act ("PIA") 2021, there is now more certainty around upstream investments in the industry. Thus, one can safely conclude that despite its imperfections, the passage of the PIA was a step in the right direction. This is, however, not sufficient to drive the sort of investments the majors/ international oil companies (IOCs) require. Hence, government does need to do much more to improve the attractiveness of the upstream sector, to not just the juniors and or independents. Government should also consider more engagements with the majors/IOCs to be better able to determine what they require to commit risk capital in Nigeria.

In the power sector, the regulator needs to forge a delicate balance between enforcing regulations and not over-regulating. The private sector should be encouraged to do more off-grid projects with minimal interference from NERC. NERC should resist the temptation to over-regulate whilst also ensuring that regulatory capture does not become the norm. Sub-franchising should be entrenched, and metering should be 'forced' if that's the only way same will succeed.

The regulator should enforce regulation, and ensure the Discos use technology, to reduce electricity theft. This should work together with sub-franchising and proper metering. The government should also do its utmost to see the Siemens deal through.

Issues, such as obtaining import duty exemption certificates should be made easier and more straightforward, such that the incentives usually touted by the government and regulators are not just proposed in theory but can be easily obtained. Government does need to also continue to work very hard to substantially improve the security situation in the country as foreigners will not invest in a substantially unsafe environment or country. The narrative, around security, ought to substantially improve to further drive investment.

The foregoing challenges, notwithstanding, there are opportunities across the entire energy sector value chain for interested persons. Nigeria's large populations remains a very attractive proposition and with the communal living system, there will always be demand for high quality products, goods, and services in the energy sector. Notably, the midstream and downstream sectors (especially downstream) thrive on margins and volumes, and so with the huge Nigerian population, these opportunities are there for the taking by discerning business persons.

There are opportunities for private investors to acquire government assets to be sold (such as the NIPP Plants), opportunities for industry players to invest in different areas of the energy value chain, and of course, for industry experts, including lawyers, to advise private players and government, amongst others. Services may also be rendered, and finders' fees received for helping connect counterparties, amongst others.

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