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Kenya:

An African oil upstart in transition

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Executive Summary

In late March 2012, Kenya entered the East African oil scene with a surprising splash. After decades of unsuccessful on-and-off exploration by international oil companies, Tullow Oil, a UK-based firm, discovered oil in Kenya's north-west Turkana County. This paper analyses the opportunities and risks facing Kenya's oil industry and its role as a regional oil transport hub. It provides a snapshot of Kenya's economic, political, and security environment, offers a comprehensive overview of the development of Kenya's oil industry and possibilities for regional oil infrastructure cooperation with neighbouring countries in East Africa, and considers the potential political, social, and security risks facing the oil industry and regional infrastructure plans.

Kenya Overview

In the aftermath of the large-scale violence that followed its December 2007 general elections, Kenya has turned a corner. In June 2008 its government launched Vision 2030, an ambitious development blueprint, to modernize and make Kenya a middle-income economy; in 2010 it passed a new constitution; and in 2013 contested, yet largely peaceful, general elections were held. The discovery of oil in 2012 immediately provided an extra boost to Kenya's already growing and diverse economy and its position as East Africa's strategic transport and communications hub.

But over the past two years, political and security tensions have risen dramatically to threaten Kenya's bright future. In the political arena, the 2010 constitution stipulated the devolution of powers from the central government to newly constituted counties, but its full realization must overcome enormous systematic, structural, and political implementation hurdles. At the same time, devolution will hardly be a success if it only leads to the decentralization of Kenya's political troubles (which include ethno-politics and corruption) to the local level, where more political officials are now in competition with one another. Oil and other resources will influence disputes between central authorities and counties and communities seeking to assert new-found powers.

On the security front, terrorist attacks, highlighted by the September 2013 killings by the Somalia-based militant group al-Shabaab at Nairobi's upscale Westgate Shopping Mall, have grown in Kenya's coastal and north-eastern regions. These attacks threaten to enflame and intermingle with long-standing animosities between communities in these regions and the central government in Nairobi, undermining the popular development aspirations introduced by the new constitution. Possible insecurity from political and social tensions sits ominously alongside the oil industry's plans to move from the exploration to development phase and to construct key export infrastructure on the coast.

Kenya's oil sector and regional infrastructure cooperation

Kenya's role as a regional hub for East African crude oil and petroleum products may be more significant than its potential position as an oil and gas producer. To date, Kenya's oil resources are estimated to be 600 million barrels and new discoveries may still only make the country a small African producer. Oil exploration in Kenya began in the 1950s with Shell and BP carrying out the first survey work, mapping out major geological basins, and drilling the first oil well in 1960. Over 40 wells have since been drilled on and offshore, but it was not until 2012 that potential commercially viable oil resources were discovered through Tullow Oil's Ngamia 1, together with subsequent findings in Turkana County in Kenya's north-west.

Recent interest grew out of Uganda's 2006 onshore oil discoveries, and offshore gas findings in Mozambique and Tanzania. The regional proximity of proven oil and gas reserves, coupled with sustained high international oil prices, attracted a wide variety of oil companies to Kenya; these included Africa Oil, Tullow Oil, BG Group, and Total. Tullow is seeking to finalize appraisal and testing of an estimated 600 million barrels of oil resources held in Turkana by the end of 2015. At that point, if the discoveries prove to be commercially viable, the company aims to also settle plans with the Kenya government for an export pipeline to the coast at either Lamu or Mombasa.

However, the huge and diverse infrastructure development goals of Kenya's $25 billion Lamu Port, South Sudan, Ethiopia, Transport (LAPSSET) Corridor will be significantly delayed and likely need to be downsized. A piecemeal approach – beginning with a basic export pipeline and port terminal at Lamu – may well be adopted. Rather than Kenya joining Ethiopia and South Sudan in plans for export and product pipelines to Lamu, it is more likely that, in the short term, Uganda and Kenya will establish the first pipeline links while other neighbours join through oil, road, and rail links in the medium and long term.

Kenya could go it alone and develop an 850 kilometre export pipeline from Turkana to the coast for its oil resources, but since its findings still remain relatively small, a regional agreement with Uganda to share an oil pipeline would be more viable. But there remain hurdles to achieving such cooperation. It will take two to four years to ascertain final commerciality of Kenya's oil discoveries and in the meantime Uganda remains eager to push forward with generating revenues from its long idle but proven oil reserves.

Political, social, and security risks

As the oil industry shifts from exploration to development and production in Kenya, required investments will grow from hundreds of millions to billions of dollars for new oil infrastructure. Tullow Oil, and in particular its smaller and more exploration-orientated partner Africa Oil, will likely sell a share of their interests in the Turkana concessions to larger industry players, such as oil majors and Asian national oil companies, to provide the required capital investments to develop the oil fields. It is at this juncture that risk incentives among the involved oil companies will decline profoundly. During the exploration phase, in the initial drive to discover oil, oil industry operations have been left relatively free from regulatory constraints and political interference. In the upcoming development and production phase this will likely not be the case. The nascent oil industry will not be completely insulated from increased risks in a shifting political and security landscape.

First, the regulatory environment for the oil industry in Kenya is in flux. The establishment and implementation of a new National Energy Bill and Petroleum Exploration and Development Production Act will have important consequences for the oil industry. New laws will encourage investment on one hand, particularly in natural gas where there is a lack of regulation, but on the other hand such laws can increase the costs of doing business. And since the political and regulatory environment in Kenya is intertwined, the government may exploit new rules and regulations to advance political and economic goals. Once production does begin, and petrodollars flow into government coffers, oil revenue sharing will become a fixture of Kenya's often-divisive politics.

Second, the successful advancement of the 2010 constitution offers potential economic and social development benefits and help in reversing high levels of inequality in Kenya. Such a process, however, offers challenges to the oil industry as communities in oil regions, and their political representatives, grapple with the convergence of new economic resources and increased political power through devolution. But a failure by the Kenyan government to implement devolution could be even more damaging to the timely development of the oil industry. Such an outcome could see aggrieved counties contest oil resources with the national government and international oil companies. If the objectives of devolution in the new constitution are fulfilled and political power and economic resources shift from the centre to county level (particularly in restless peripheral regions such as Turkana) then conflicts over scarce resources can be mitigated.

Third, political instability and insecurity is threatening not only the commencement of Kenya's oil production, but also its exit to international markets on the coast. Kenya's coastal and north-eastern communities have longstanding social and political grievances with the central government in Nairobi. Internal politics alone has the capacity to create insecurity for the oil industry if planned pipeline and other downstream infrastructure are targeted. But there is also the possibility that these disputes could become a toxic mix with the incursion of the Somalia-based militant group al-Shabaab, delaying and hampering large-scale investments.

Al-Shabaab may be positioning itself to exploit social and political tensions to win support from local populations on Kenya's coast. But if the Kenyan government is able to advance political devolution to coastal counties, while working to contain al-Shabaab in an apolitical manner, then there is a strong likelihood that, with regional and international support, Nairobi can curb the militant group's activities, providing the oil industry with a relatively secure environment. If Kenya is to become the transit hub for East Africa's oil boom then relative stability and security on the coast must be achieved.


KENYA
National capital
Provincial capital
Town, village
Airports
International boundary
Main road
Secondary road
Other road or track
Railroad
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SOUTH SUDAN
Administrative Boundary
ETHIOPIA
UGANDA
SOMALIA
UNITED REPUBLIC OF TANZANIA
INDIAN OCEAN
Lake Turkana (Lake Rudolf)
Lake Chew Bahir
Sibiloi National Park
Lake Victoria
Lake Natron
Ungama Bay
Nairobi
Mombasa
Kisumu
Nakuru
Eldoret
Kakamega
Nyeri
Embu
Garissa
Mt. Kenya 5199 m
Kilimanjaro 5895 m
Lodwar
Lokichokio
Kakuma
Lokichar
Lokori
Marsabit
Moyale
Mandera
Wajir
Isiolo
Meru
Thika
Machakos
Kitui
Malindi
Kilifi
Lamu
Voi
Tsavo
Narok
Kericho
Kitale
Naivasha
Tana
Galana
Athi
0 50 100 150 200 km
0 25 50 75 100 mi

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Introduction

In late March 2012, Kenya entered the East African oil scene with a surprising splash. After decades of unsuccessful on-and-off exploration by international oil companies, Tullow Oil, a UK-based firm, discovered oil in Kenya's north-west Turkana County. Quite unceremoniously, then President Mwai Kibaki announced the find at the end of a planned speech on performance evaluation results for public agencies: 'I wish to make an important announcement to the nation ... This morning, I have been informed by the Minister for Energy that our country has made a major breakthrough in oil exploration … This is the first time Kenya has made such a discovery and it is very good news for our country. It is, however, the beginning of a long journey to make our country an oil producer…'[1]

This paper analyses the opportunities and challenges facing Kenya's oil industry and role as a regional oil transport hub. First, it provides a snapshot of Kenya's political and economic environment. Second, the paper offers a comprehensive overview of the development of Kenya's oil industry, from exploration to the upcoming production phase, the main players, and the possibilities for regional oil infrastructure in cooperation with neighbouring countries in East Africa. Finally, the paper considers the potential political risk from new rules and regulations, the social risk from relations with local communities and officials in Turkana County (where oil has been discovered), and the security risk facing oil industry and regional infrastructure plans. The paper does not fully engage questions revolving around the 'resource curse' in Africa – concerning how oil will impact Kenya's economic, political, and social development. Rather it does the reverse, by examining how Kenya's political economy and security environment will impact the industry in the future.

Kenya Overview

Economic aspirations

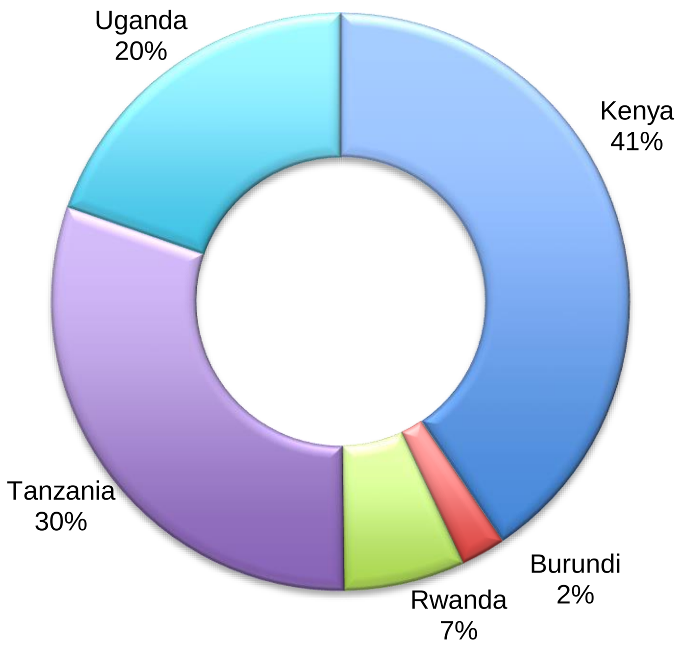
Kenya is the economic centre of East Africa. It has the largest economy in the East African Community (Figures 1 and 2) and one of the largest in Africa. It also has one of the most diverse economies on the continent. Tea, coffee, and other agriculture, alongside tourism and services, are a major part of Kenya's economic success story (Figure 3). This is in sharp contrast to other large African economies where oil, gas, and minerals dominate. On the back of growth in tourism and telecommunications, Kenya enjoyed average annual growth rates of 5.4 per cent between 2002 and 2007.[2] The economy was unsettled by the insecurity that followed the 2007 general elections, but it has picked up pace again in recent years. In 2014, international investors demonstrated their confidence in the economy when Kenya raised $2 billion in its first sovereign bond offering, a record-breaking debut for an African country.[3]

[1] 'Speech by his excellency Hon. Mwai Kibaki, C.G.H., M.P., President and Commander-in-Chief of the defence forces of the Republic of Kenya during the official announcement of the evaluation results of the performance of public agencies for the financial year 2010/11', Kenyatta International Conference Centre, Nairobi, 26 March 2012, statehousekenya.go.ke, accessed 23 July 2014.

[2] Geir Sundet & Eli Moen, 'Political Economy Analysis of Kenya', Norwegian Agency for Development Cooperation, Oslo, 2009, 10.

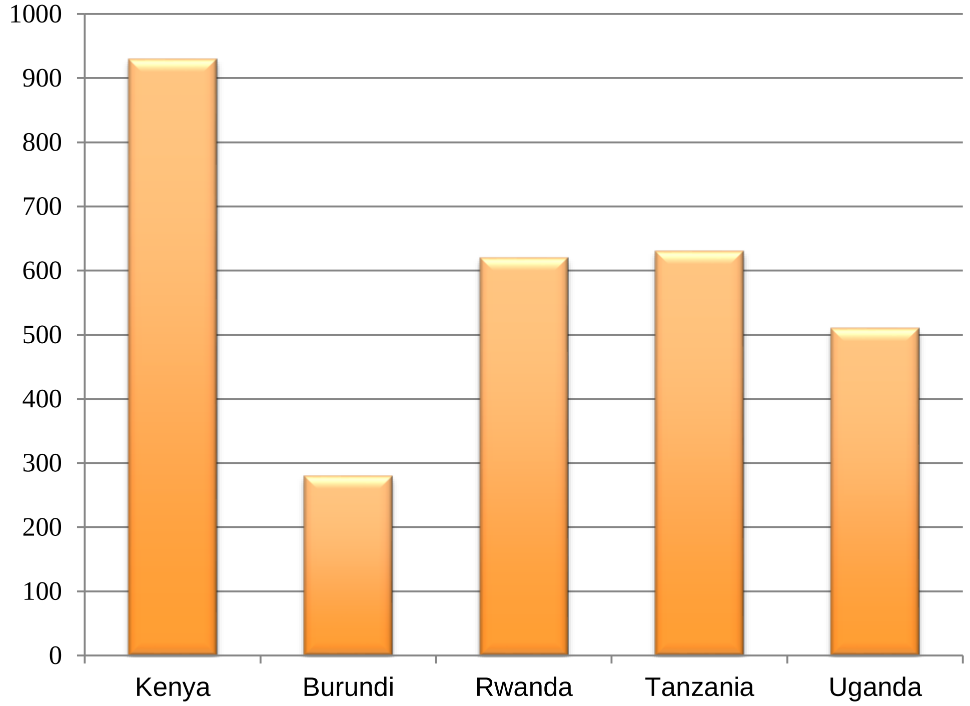
[3] Katrina Manson & Javier Blas, 'Kenya's debut $2bn bond breaks Africa record', *Financial Times*, 16 June 2014.

Figure 1: East African Community – GDP billion (USD, 2013)



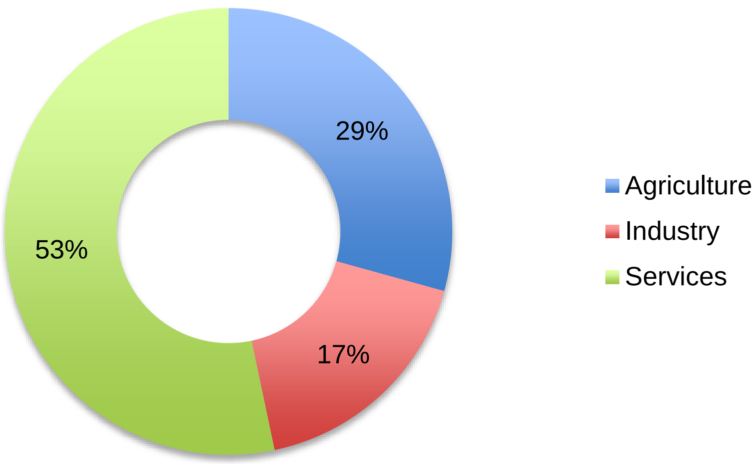
Source: World Bank

Figure 2: East African Community – GNI per capita (USD, 2013)



Source: World Bank

Figure 3: Economic Structure, Kenya 2013



Source: CIA – The World Factbook

Kenya's economic strength is bolstered by its strategic position in East Africa. It is the main entry and exit point for trade from landlocked East and Central African countries – Uganda, Rwanda, Burundi, and South Sudan. Uganda was its largest export partner in 2013, accounting for 13.6 per cent of total Kenyan exports.[4] Mombasa is East Africa's largest port, followed by those in Tanzania and Djibouti. Kenya is seeking to exploit its strategic location on the Indian Ocean further by leveraging its relative proximity to large and growing Asian markets, particularly those in India and China which are Kenya's largest import partners, representing 14.2 per cent and 12.2 per cent respectively of total imports in 2013.[5] Kenya is also the financial and communications hub for East Africa. 'Silicon Savannah', an initiative to establish a major techno-city in Konzo, 40 miles outside Nairobi, seeks to make Kenya East Africa's technology hub as well. IBM established its first African research lab in Nairobi, while Google, Microsoft, and Intel also have regional headquarters there.[6]

Kenya's diversified economy needs substantial infrastructure development in order to industrialize. In 2008, the Kenyan government under then President Mwai Kibaki established Vision 2030 to modernize Kenya and make it a middle-income country. One of the flagship projects of the initiative is the $25 billion Lamu Port, South Sudan, Ethiopia, Transport (LAPSSET) Corridor. This seeks to establish road, rail, and oil pipeline links between the regional neighbours, airports, and resort cities at Isiolo and Lamu, as well as a new port at Manda Bay and a 120,000 barrels/day (b/d) oil refinery at Lamu.[7] The twin goals of this ambitious undertaking are to promote regional economic development and to develop northern Kenya (which has long been economically marginalized compared to central counties) and integrate it into the national economy.

Although there has been little progress in its implementation since the 2012 official launch of LAPSSET,[8] Kenya is also spearheading other related regional infrastructure agreements. President Uhuru Kenyatta hosted Chinese Premier Li Keiqiang in May 2014 and, alongside regional leaders

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[4] Economist Intelligence Unit, 'Kenya', Country Report, EIU, London, 1 June 2014.
[5] Economist Intelligence Unit, 'Kenya', Country Report, EIU, London, 1 June 2014.
[6] Mwangi S. Kimenyi & Josephine Kibe, 'Africa's Powerhouse', Brookings, Opinion, 6 January 2014 www.brookings.edu/research/opinions/2013/12/30-kenya-economy-kimenyi, accessed 28 July 2014.
[7] 'Lamu Port and New Transport Corridor Development to Southern Sudan and Ethiopia (LAPSSET)', Progress Report, Kenya Vision 2030, Government of the Republic of Kenya, www.vision2030.go.ke.
[8] Drazen Jorgic, 'Kenya attacks undermine plans for east African trade hub', *Reuters*, 20 June 2014.

from South Sudan, Rwanda, and Uganda, signed an agreement to establish a new East African railway line. At nearly $4 billion, Chinese companies will build the first stage, a 610-kilometre line from Mombasa to Nairobi.[9] As a sign of Kenya's broadening international ties, the planned Chinese-built railway will replace the original line established during British colonial rule over 100 years ago. If Kenya is to continue to act as the gateway to East Africa in the face of outside competition (Tanzania is busy enhancing its own ports with Chinese cooperation), then such infrastructure projects will need to move forward.

The discovery of oil could help Kenya finance its large infrastructure needs. The current government, under Uhuru Kenyatta, included oil, gas, and mineral resources as a sixth priority sector within the economic pillar of Vision 2030; this seeks to harness oil to increase export earnings and produce higher GDP growth, broader social development, infrastructure development, and job creation.[10] The oil industry needs billions in infrastructure development investment if it is to act as a driver for Kenya's broader economic and social development goals. But over the past two years political and security tensions have risen dramatically, threatening to upend Kenya's economic aspirations.

Political and security challenges

It had been expected that 2013 would be a breakout year for Kenya – the country was turning a corner after having held largely peaceful general elections in March that year. Its new Jubilee government may have been dogged by the indictment of President Uhuru and Deputy President Ruto by the International Criminal Court (ICC) for their alleged role in the 2007/08 post-election violence, but a resurgent economy gave promise for the future. Jubilee pushed forward with former president Kibaki's Vision 2030 to modernize Kenya; the government was generally business friendly, engaging a younger generation of industrialists and entrepreneurs compared to previous governments.[11]

But 2013 would not be the year of stability and growth for which Kenya had hoped. The 2010 constitution stipulated the devolution of powers from the central government to newly constituted counties, but its full realization needed to overcome enormous systematic, structural, and political implementation hurdles. All the while terrorist attacks – prominent among which was the September 2013 massacre carried out by the Somalia-based militant group al-Shabaab at Nairobi's upscale Westgate Shopping Mall – have grown in Kenya's coastal and north-eastern regions. These attacks threaten to enflame and intermingle with long-standing animosities between communities in these regions and the central government in Nairobi, undermining the popular development aspirations put forward by the new constitution.

Oil and other resources will influence disputes between central authorities and counties and communities seeking to assert new-found powers stipulated by the constitution. Possible insecurity due to political and social tensions sits ominously alongside the oil industry's plans to move from the exploration to the development phase, combined with construction of key export infrastructure on the coast. The insecurity has hurt Kenya's tourism sector, one of its main economic engines and job producers. The World Bank downgraded its forecast on economic growth in 2014 and 2015 from 5.2 per cent to 4.7 per cent for both years on account of the insecurity.[12] A failure to grapple with these structural problems through fully implementing devolution, to settle the ICC indictment, and to tackle terrorism will undermine development.

Kenyan politics are ethnically and regionally-driven and are deeply embedded in business. Kenya has been described as an 'ethnocracy'; a democracy in which politics are steered along ethnic lines and

[9] 'China to build new East Africa railway line', *BBC News*, 12 May 2014.

[10] 'Second Medium Term Plan 2013-2017', Kenya Vision 2030, Government of the Republic of Kenya, Nairobi, 2013, 68.

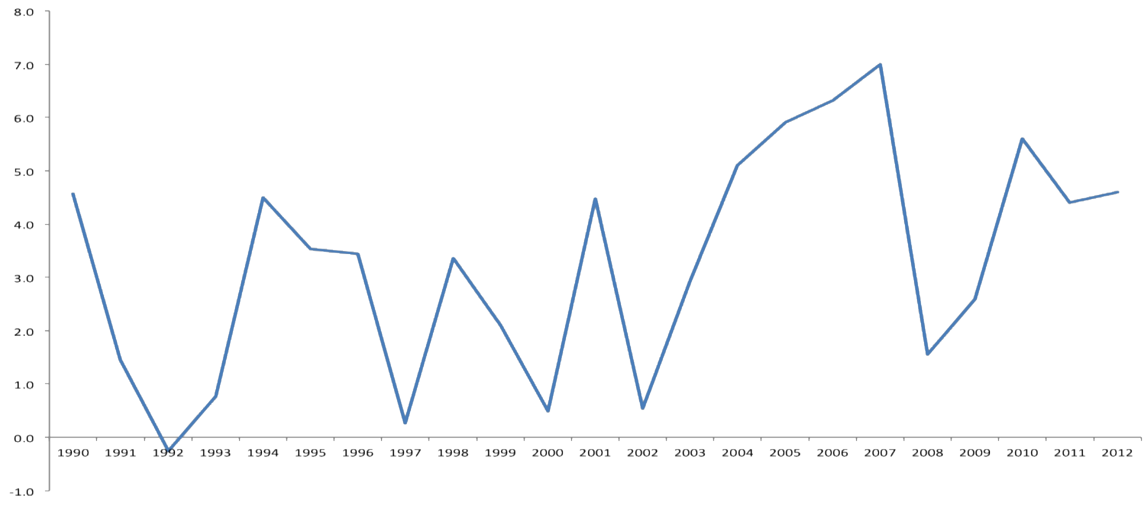
[11] David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 22.

[12] David Malingha and Sarah McGregor, 'East Africa Powerhouse Kenya Shaken as Attacks, Politics Mix', *Bloomberg*, 8 July 2014.

coalitions, or 'tribal arithmetic' applied to form and structure the government.[13] The political culture is a product of the manner in which the British colonial administration limited political organization to specific regions in Kenya, to avoid the establishment of national movements; this served to ethnocize Kenyan politics early on.[14] The Kikuyu, roughly representing 20 per cent of the population, were the dominant group after Kenya's 1963 independence and remain so today. Kenya's first president, Jomo Kenyatta, the father of the current president Uhuru, established a patrimonial state where informal networks which formed around the president and ruling party rewarded clients with land, state contracts, and other preferential treatment.[15] After Daniel arap Moi became president in 1979, he set about shifting the centre of political and economic power away from the Kikuyu community and towards his Kalenjin community and Kenyan Asian business allies.[16] In 2002, the Kalenjin–Kenya–Asia alliance lost its strong position in politics and business after a coalition of opposition parties led by Mwai Kibaki, a Kikuyu, rose to power. This brought central political influence back to the Kikuyu community.

The political violence that followed the 2007 general elections dealt a serious blow to Kenya's political stability and growing economy. More than 1,000 people were killed and 650,000 displaced in the post-election ethnic fighting, which was mainly between Kenya's largest groups, the Kikuyus, Kalenjins, and Luo. An African Union mediation team led by former United Nations Secretary General Kofi Annan was able to broker a coalition government between President Kibaki and opposition leader Raila Odinga. But this was not the first time that election outcomes had sparked widespread violence and economic decline, political violence has been the norm rather than the exception in the lead up to and aftermath of Kenyan elections.[17] Since multiparty elections were established in 1992, the economy has suffered from periodic bouts of violence (Figure 4).

Figure 4: Kenya's annual growth rate (%) – illustrating economic decline and multi-party elections (1992, 1997, 2002, 2007)



Source: David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 30.

[13] Jeffrey Gettleman, 'Kenya's Future Clouds as Tensions Rise and Tourists Flee', *The New York Times*, 27 June 2014.
[14] Geir Sundet & Eli Moen, 'Political Economy Analysis of Kenya', Norwegian Agency for Development Cooperation, Oslo, 2009, 6.
[15] Geir Sundet & Eli Moen, 'Political Economy Analysis of Kenya', Norwegian Agency for Development Cooperation, Oslo, 2009, 1.
[16] David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 13–15.
[17] Geir Sundet & Eli Moen, 'Political Economy Analysis of Kenya', Norwegian Agency for Development Cooperation, Oslo, 2009, 8.

The coalition government formed in 2008 succeeded in passing a new constitution in 2010; this strived to change the way in which Kenyan public affairs are managed and to repair the country's ethnocized and oft-violent political culture. It sets out to devolve political and economic decision-making from the presidency to 47 new counties throughout the country (Figure 5). The aim is to reverse the high regional inequalities and ethnic tensions that have mired politics and sparked violence since independence. These institutional changes are geared towards making government officials more accountable to local populations and addressing deep inequalities and grievances; between 2000 and 2010 Kenya's inequality levels were some of the worst in the world – higher than other budding African oil and gas producers such as Uganda, Mozambique, and Tanzania.[18] The restructuring of the entire fabric of how politics and business have functioned in Kenya for over a half century was to be a challenging endeavour.

In the 2012 general election then Prime Minister Raila Odinga faced off against Uhuru Kenyatta. It was again a close and contested election, but Uhuru prevailed and The National Alliance party formed a new government – the Jubilee Alliance – with William Ruto, a Kalenjin, leading the United Republican Party, as deputy president. Both Uhuru and Ruto were indicted by the International Criminal Court for their alleged role in inciting post-election violence in 2007/08. The ICC prosecutor's case, however, has been weakened by the retraction of statements and deaths of key witnesses, but the indictments may still drive a wedge between Uhuru and Ruto's political camps.[19]

While international oil companies are concerned about legal measures which may be taken by western governments if Kenya's leaders are convicted, in all likelihood Kenya's relationship with the USA and Europe will remain strong due to mutual regional security concerns revolving around al-Shabaab and other militant groups operating out of Somalia.[20] Kenya has, nonetheless, rebounded from the strained diplomatic relations with western countries caused by the ICC indictments to look east to China and other non-western partners for new avenues of economic engagement. Balancing between foreign partners, however, will not solve political divides at the national level.

The 2013 election outcome was no exception in Kenya's historical political trend. Kenyan politics remains polarized along ethnic-regional lines, with the Kikuyu/Kalenjin Jubilee Alliance in government and Odinga's CORD Alliance of Luo, Kamba, Luhya, and coastal groups in opposition.[21] Political tensions, corruption, poverty, and high levels of inequality are also still very real, and very challenging, hurdles to overcome. Devolution will remain a central feature of Kenya's political landscape in the coming years, especially in the lead up to new elections in 2017.[22] Important political questions on whether central authorities will fully implement institutional changes remain unanswered, as the process is in its early stages. At the same time, whether or not the counties will have the capacity and expertise to manage their new-found power is also unclear.

Devolution may only lead to the decentralization of Kenya's political troubles, including ethno-politics and corruption, to the local level, where more political officials are now in competition with one another. What is clear is that a failure to push forward with devolution and other key aspects of the new constitution by the central government will only heighten political tensions. But if Uhuru and Ruto were to move forward with implementing the new constitution, progress towards a more inclusive government is possible; this would strengthen the government's hand with both local constituents and western partners. The oil industry is set to develop midst this shifting political and security environment.

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[18] Patricia I. Vasquez, 'Kenya at a crossroads: Hopes and fears concerning the development of oil and gas reserves', *Articles and Debates*, 4.3, International Development Policy, Graduate Institute of International and Development Studies, 2013, 7.

[19] 'Kenya, Chickens come home to roost', *Africa Confidential*, Vol. 55, No. 1, 10 January 2014.

[20] Andrea S. Pongo, 'Effects of the 2013 National Elections on Oil Exploration in Kenya', Institute for Defense Analyses, Alexandria VA, 2013, 7–8.

[21] David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 27.

[22] David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 31–2.

Figure 5: Kenya's new political constituencies

Source: Kenya Open Data, Government of Kenya

Kenya’s oil sector and regional infrastructure cooperation

Kenya’s long history of oil exploration has come in three waves. BP and Shell began the first exploration work in the 1950s. Aeromagnetic, gravimetric, and seismic surveys identified over 300,000 square kilometres of sedimentary basin: the Tertiary Rift Basin to the north-west, Anza in the north, Mandera in the east, and Lamu, which is both on and offshore, in the south-east.[23] BP and Shell also drilled the first well in 1960 in the Lamu embayment. In the 1970s, Kenya continued to attract attention in the international oil industry as oil majors looked for alternative sources of investment in the aftermath of major nationalizations in the Middle East, North Africa, and Latin America. Altogether, a total of 15 wells were drilled in Kenya throughout the 1960s and 70s, but with no commercial success.

The second wave of oil exploration came after Kenya established its Petroleum Act in 1985. This encouraged new investment by changing previous royalty-based contracts to production-sharing contracts.[24] Another 15 wells were drilled in the 1980s and 90s. Among other companies, Total and Amoco were most active in exploration work. They drilled in Anza and Mandera basins, discovered indications of oil and gas, but no commercial finds. In 1992, the Loperot-1 well was drilled in Block 10BB by Shell some 100 kilometres south of the town of Lodwar in present-day Turkana County. This showed signs of waxy crude, but Shell abandoned its work after failing to negotiate a contract extension with the Moi government, which took power that year. Low international oil prices in the mid and late 1980s provided little incentive for expensive exploration and development work.

The third and current wave of exploration in Kenya’s oil industry came in 2000, after the Kenyan government had carried out new geological studies on the Lamu and Tertiary Rift basins.[25] Interest grew substantially after Uganda’s 2006 onshore oil discoveries, and offshore gas finds in Mozambique and Tanzania. The regional proximity of proven oil and gas reserves, coupled with sustained high international oil prices, attracted a wide variety of oil companies to Kenya, these included: Africa Oil, Apache Corporation, Anadarko, BG Group, Centric, Cove Energy, Pancontinental, Premier Oil, Simba Energy, CNOOC, Total, and Tullow Oil (Figure 6). By 2012, a total of 33 wells had been drilled onshore, half of which showed signs of hydrocarbons, as well as four non-commercial wells offshore.[26] But it was not until Tullow’s Ngamia 1 discovery in early 2012, together with a string of others in Block 10BB and Block 13T in Turkana County, that oil resources of significant commercial potential were found.

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[23] ‘Untapped Oil Frontier: Hunting Elephants in East Africa’, *Cormark Securities Inc*., 3 February 2011, 15–7.

[24] ‘Overview of Petroleum Exploration in Kenya’, Presentation to the 5th East African Petroleum Conference and Exhibition 2011, Ministry of Energy, Kenya, 25 February 2011, 6.

[25] ‘Setting the Agenda for the Development of Kenya’s Oil and Gas Resources – The Perspectives of Civil Society’, The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 14.

[26] Deloitte, ‘The Deloitte Guide to Oil and Gas in East Africa: Where potential lies’, *Deloitte*, 2013, 4.

Figure 6: Licensed Petroleum Exploration Companies in Kenya as of June 2014

No	Exploration Companies	Exploration Block Nos.	No. Of Blocks
1.	Tullow Oil Corporation	10A, 10BB, 10BA, 13T, 12A, and 12B	6
2.	Anardarko	L-5, L-7, L-12, L-11A, L-11B	5
3.	BG Group	L-10A, L-10B	2
4.	Ophir/Dominion	L-9, L-5	2
5.	Apache (now withdrawn)	L-8	1
6.	Vanoil Resources	3A, 3B	2
7.	Africa Oil Corporation	9	1
8.	Zarara	L-4, L-13	2
9.	FAR/Flow Energy	L-6	1
10.	Lion Petroleum	2B	1
11.	NOCK	14T	1
12.	Simba	2A	1
13.	Afren	L-17/L-18, 1	3
14.	A-Z Petroleum	L-1A & L-3	2
15.	CAMAC Energy	L-1B, L-16, L-27, L-28	4
16.	Rift Energy	L-19	1
17.	Imara Energy Corp.	L-2	1
18.	Adamantine Energy Ltd	11A	1
19.	Pacific Seaboard Investments Ltd	L-20	1
20.	ERHC Energy Inc.	11B	1
21.	Lamu Oil Exploration	L-14	1
22.	Total Exploration & Production Kenya B.V.	L-22	1
23.	ENI Spa	L-21, L-23, L-24	3

Source: 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 17.

Exploration

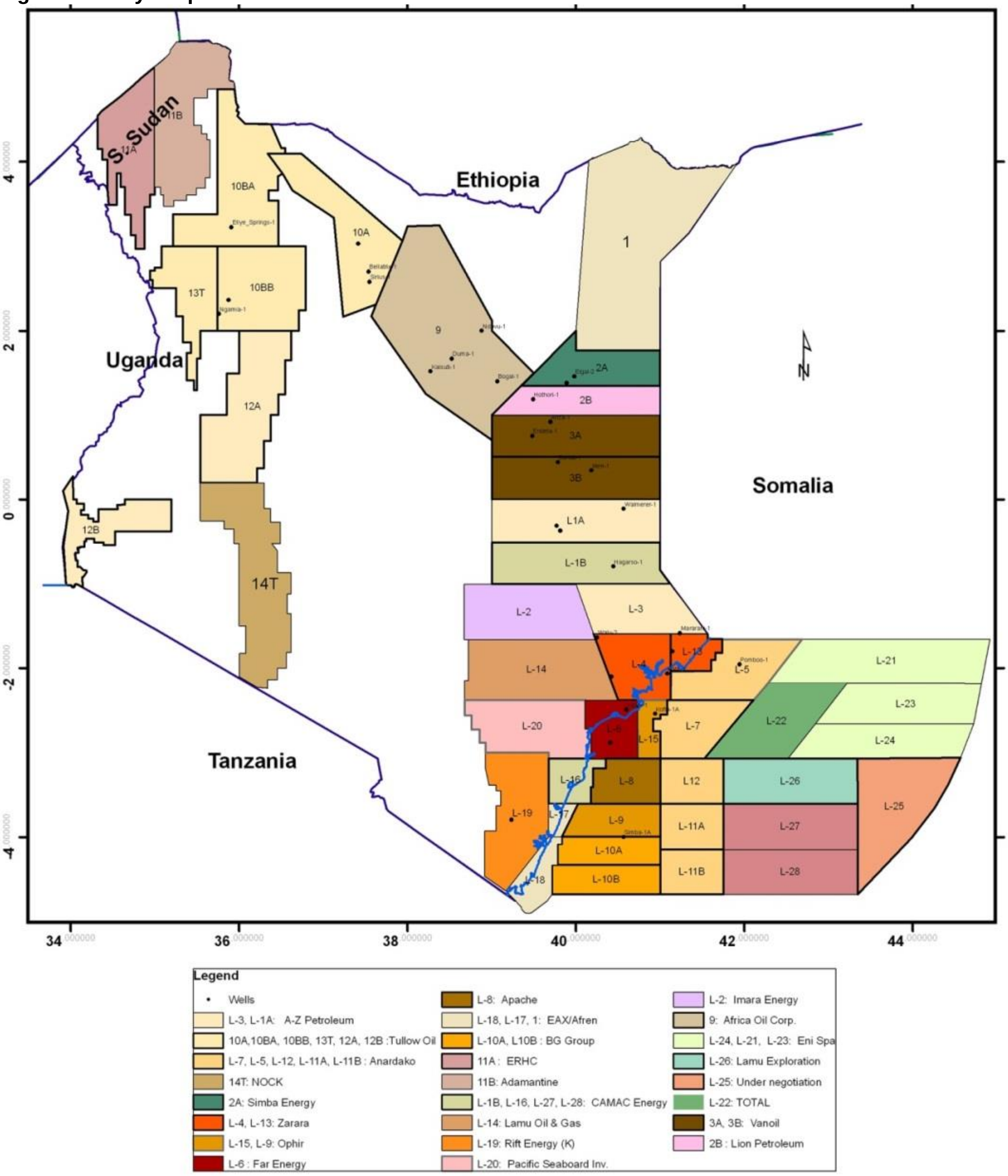
Kenya is an attractive investment location in the global oil business, particularly for upstart mid-sized oil companies and Asian national oil companies looking to increase their international activities. Sentiment remains upbeat for new finds in Kenya's oil and gas concessions (Figure 7). As Africa Oil CEO Keith Hill has said: 'There are not many places left on earth where you can put together an acreage portfolio like this ... Good contract terms, good support from the government – there are not that many happy hunting grounds left'.[27] Africa Oil, as part of the Lundin Group, has a longer history in Kenya than most international oil companies. Lundin entered Kenya in late 2007, after signing a contract in Block 10A in the Anza Basin, in the north. (Anza is an extension of the Muglad Basin in South Sudan, where Lundin was once active.[28]) Lundin then bought an interest in Block 9, also in Anza, from the China National Offshore Oil Corporation (CNOOC), a state-owned oil company. In 2009, Lundin sold its Kenya interests to Africa Oil, in which it was a majority shareholder.[29]

CNOOC had arrived in Kenya in 2006. It signed six contracts with Kenya in the Lamu, Anza, and Mandera Basins in a well-publicized ceremony attended by China's President Hu Jintao and Kenya's Mwai Kabiki.[30] The political pomp, however, did not help CNOOC find oil, although it drilled the over 5,000 metre deep Bogal 1 well in Block 9 in 2009, at a cost of $25 million. This was the deepest well ever drilled in Kenya,[31] and while it confirmed there was hydrocarbon potential in Anza, no oil was found. In 2010, CNOOC left Kenya to invest $1.45 billion into Uganda's proven oil reserves with Total and Tullow. Africa Oil, also a partner in Bogal 1, has not abandoned Block 9; it is re-evaluating CNOOC data and planning Bogal 2 in search of gas.[32]

In hopes of repeating the natural gas discovery story of Mozambique and Tanzania, the Kenyan Ministry of Energy was quick to establish new offshore deepwater concessions.[33] In addition to a number of mid-sized exploration companies, the French oil major Total was attracted to the prospects and bought a 40 per cent stake in a number of Anadarko's and Cove Energy's concessions in 2011 (L5, L7, L11a, L11b, and L12) in the Lamu Basin. Total then acquired 100 per cent of offshore block L22 the following year, but exploration wells drilled in Blocks L7 and L11b did not produce positive results.[34] After Apache drilled its Mbawa 1 well in 2012 in Block L8 it did encounter gas, but abandoned the concession in late 2013.[35] While offshore gas has still not been discovered in commercial quantities, the BG Group and its partners found both oil and gas offshore in Lamu in 2014 and are assessing the commercial potential.[36] Drilling an offshore well in Kenya typically costs $80 million, but if BG's results prove positive, this may help to incentivize further exploration into Kenyan waters.

[27] Yadullah Hussain, 'Canada's Africa Oil Corp. sees promise in Kenya', *Financial Post*, 24 October 2013.
[28] Daniel Wells, 'Sweden's Lundin signs Kenya oil exploration deal', *Reuters*, 8 October 2007.
[29] Africa Oil bought these interests with a loan provided by Lundin; 'Lundin Petroleum to sell its East African interests', Lundin Petroleum, 5 February 2009, www.lundin-petroleum.com/Press/pr_corp_05-02-09_e.html, accessed 28 July 2014.
[30] 'CNOOC signs deal to search for oil in Kenya', *CRIENGLISH.com*, 29 April 2006, http://english.cri.cn/811/2006/04/29/301@83073.htm, accessed 28 July 2014.
[31] 'Untapped Oil Frontier: Hunting Elephants in East Africa', *Cormark Securities Inc*., 3 February 2011, 17.
[32] 'Kenya Joins East Africa Oil and Gas Frenzy', *Energy Intelligence Finance*, 4 April 2012.
[33] 'Kenya Joins East Africa Oil and Gas Frenzy', *Energy Intelligence Finance*, 4 April 2012.
[34] Total, '2013 Form 20-F Total S.A.', Total, Paris, 17–18
[35] Eduard Gismatullin, 'Apache Exits Kenya to Focus on Energy Exploration Elsewhere', *Bloomberg*, 9 October 2013.
[36] Kennedy Senelwa, 'BG to submit plans after Lamu oil find', *The East African*, 21 June 2014.

Figure 7: Kenya exploration blocks



Source: National Oil Corporation of Kenya

Development and production

Kenya's oil industry made a major breakthrough in 2012 with Tullow's Ngamia 1 discovery in Turkana County. Ngamia 1 helped to de-risk other prospects around Lake Turkana, opening up new exploration options.[37] Tullow first farmed into Kenya in 2010 after buying 50 per cent in Blocks 10BA, 10BB, 12A, and 13T from Africa Oil and Centric Energy. Tullow also bought into Uganda by purchasing Energy Africa in 2004, Hardman Resources in 2007, and licences of Heritage Oil in 2010. Uganda served dual purposes for Tullow's eventual entry into Kenya: it attracted the company and others due to the proximity of its discoveries, but it also benefited from the technical lessons Tullow took on from its Ugandan operations. Tullow saw analogies between the Albertine Basin in Uganda and geological features in Kenya and Ethiopia, and the company spent $23 million for licences in the two countries.[38] Sentiment (in the nature of a regional rivalry with Uganda) likely also encouraged Kenya's efforts to attract international oil companies, in order to re-energize exploration activity.[39] Uganda's 2006 oil discoveries and intervention in Somalia raised its stature in East Africa, while Kenya's position declined, alongside its economy, following the 2007/08 post-election violence. Discovering oil offered the chance to reinvigorate the economy and maintain Kenya's status as the regional economic centre.

After a year in Kenya, Tullow made multiple discoveries south-west of Lake Turkana from 2012 to 2014. Nonetheless, by mid-2014, Tullow's discoveries in Kenya remain only contingent resources, not proven oil reserves. Mwendia Nyaga Chief Executive at Oil & Energy Services Limited, a Kenyan company, has said: 'We must be cautiously optimistic ... Unless someone tells you the actual amounts they [Tullow] have discovered and stop calling the finds oil resources and start calling them oil reserves, things can go either way'.[40] Tullow plans to drill over 20 wells by the end of 2015, which will consist of new exploration and appraisal of existing finds.[41] At that point, possibilities for commercializing the oil resources will be better understood.

Tullow estimates that its finds in the South Lokichar sub-basin (within the Tertiary Basin) contain 600 million barrels of oil resources, and have the potential for 1 billion barrels.[42] Following the discoveries of Amosing 1 and Ewoi 1, Tullow's estimates had increased from 300 million to 600 million barrels from 2012 to 2014.[43] A minimum of 500 million barrels has been regarded as the threshold to satisfy onshore development costs and thus make the resources commercial.[44] Tullow estimates that production from the South Lokichar sub-basin will be above 100,000 bpd (barrels per day).[45]

In addition, good potential still remains for an upside on oil resources in Kenya. The current discoveries remain limited to the Lokichar area in Turkana County, but Tullow estimates that Kenya could hold as much as 10 billion barrels of oil.[46] Indications of slicks on the surface of Lake Turkana and oil seeps on its northern shore suggest that drilling in the lake may be another possibility,[47] although environmental and social concerns will need to be properly addressed. But some of Tullow's 2014 exploration and appraisal wells have been disappointing.[48] Kenya could very well become only a small oil producer.

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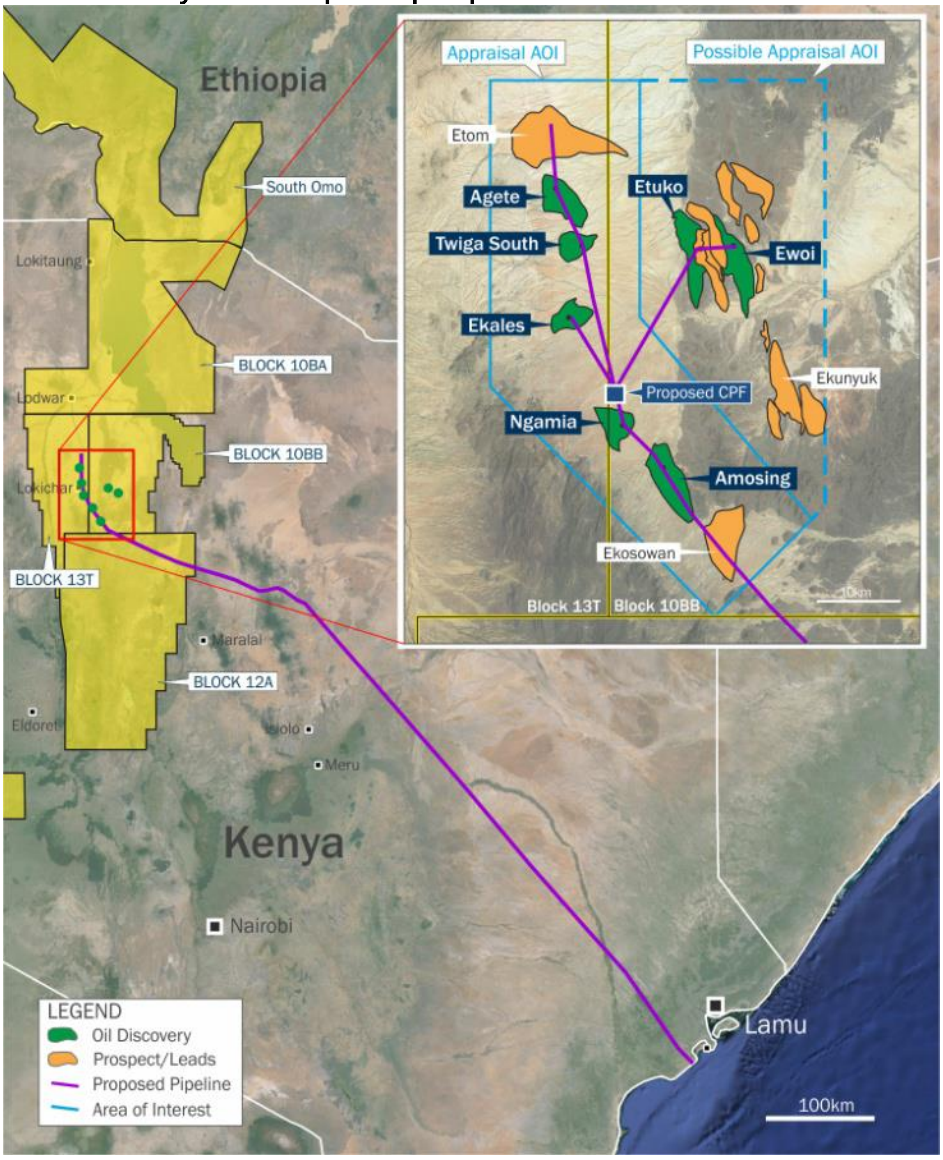
[37] 'Kenya Joins East Africa Oil and Gas Frenzy', *Energy Intelligence Finance*, 4 April 2012.
[38] 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 22.
[39] Personal communication, representative of international oil company active in Kenya, 7 September 2014.
[40] Macharia Kamau, 'Kenya could take up to five years to pump oil', *The Standard*, 17 January 2014.
[41] Tullow, 'Operational Update – Kenya', Press Release, 15 January 2014.
[42] 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 28.
[43] Macharia Kamau, 'Kenya on fast track to join world's top oil producers', *The Standard*, 16 January 2014.
[44] 'Kenya Joins East Africa Oil and Gas Frenzy', *Energy Intelligence Finance*, 4 April 2012.
[45] 'Kenya', Energy Information Agency, Country Analysis Note, April 2014.
[46] Eduard Gismatullin, 'Kenya From Nowhere Plans East Africa's First Oil Exports: Energy', *Bloomberg*, 19 August 2013.
[47] 'Kenya government approves Centric Energy farmout of Block 10BA to Tullow Oil', *Centric Energy*, Press Release, 5 November 2010.
[48] Eduard Gismatullin, 'Tullow Oil Falls Most in Two Weeks on Well Results in Kenya', *Reuters*, 27 March 2014.

Figure 8: Turkana County oil development prospects



Source: Tullow Oil, Overview Presentation, April 2014, p. 30.

Tullow and its partner Africa Oil (an exploration company) believe they can monetize the discovered oil resources. But this will prove challenging. Tullow Oil's CEO, Aidan Heavey, said in May 2013 that the company would be ready to produce if road networks were upgraded to allow for the transportation of crude oil to Kenya's Mombasa refinery.[49] This underlines the underdeveloped state of necessary infrastructure (lack of roads and railway) and the region's remoteness. As a result, getting oil out of Turkana is an expensive prospect. An 850-kilometre pipeline and supporting infrastructure is required to export Turkana's oil resources (Figure 8).[50] The quality of oil will play a role in defining Kenya's infrastructure needs. Similar to that in Uganda, the oil found in Kenya is medium light, between 25 and 35 degrees API, but waxy. The crude qualities are compatible for comingling, without having a major impact on value. But the waxy content will require the pipeline to

[49] 'Kenya ready to produce oil 'now', *Daily Nation*, 23 May 2013.
[50] 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 19.

be heated to lower the oil's viscosity, avoid the oil congealing, and allow it to flow. The pipeline will be the longest heated pipeline in the world.[51] But this is not an enviable feat, as the heating and insulation requirements will be enormously expensive. The pipeline from Turkana to Lamu on the Kenyan coast could cost up to $3 billion.[52]

In 2012, Keith Hill, CEO of Africa Oil, indicated that the company would seek to bring in larger investors to aid in developing the resource at a cost of $5 to $7 billion.[53] Total and CNOOC (each having experience in Kenya, being active, operating in partnership with Tullow in Uganda, and possessing larger chequebooks) would be obvious candidates. The pan-African Ecobank suggests that it will cost in the neighbourhood of $16 billion to develop the oil resources, construct a pipeline from Turkana to the coast, and build a new port for oil exports at Lamu.[54] Tullow wants to finalize a development plan and gain government approval for an export pipeline plan from Turkana to Kenya's coast by the end of 2016.[55] The director of the National Oil Corporation of Kenya suggests oil production could begin by 2018.[56] These may be ambitious goals, but Kenya could arguably become an oil exporter by the end of the decade.

Regional oil infrastructure development

Kenya's role as a regional hub for East African crude oil and petroleum products may be more significant than its potential position as an oil and gas producer. To date, Kenya's oil resources are estimated to be 600 million barrels. New discoveries may only make Kenya a small African producer – at the same level, if not smaller than, Uganda or Ghana. As a result, involvement in an East African oil pipeline is critical if Kenya wishes to remain the regional economic centre. Kenya can very well go it alone on oil exports and develop a pipeline to the coast from Turkana. But if both Ugandan and Kenyan oil were to run through the same pipeline network, the multi-billion dollar investment would be more viable. It is feasible to link a pipeline from Uganda's Lake Albert region, through Turkana, and onward to the coast (see Figure 9). But a significant number of obstacles remain before a regional pipeline is achieved. These include: finalizing the appraisal of discovered oil resources in Kenya, regional government approval of a pipeline plan, securing the finance, acquiring land for the route, and pipeline construction.[57] There is a long way to go before the regional pipeline can be developed and to date the neighbouring countries have been slow moving.

Progress on the Lamu Port, South Sudan, Ethiopia, Transport (LAPSSET) Corridor is a case in point, illustrating the arduous progress of regional infrastructure development in East Africa. The $25 billion flagship project of Kenya's Vision 2030 includes an oil pipeline, a 32-berth port, and a refinery at Lamu. In the 1500s, Lamu was a bustling seaport connecting routes to and from the Middle East, India, and the Far East to East Africa.[58] Whether or not it will have a modern revival remains in question. Of late, although a few preparatory developments are ongoing at the proposed port site, LAPSSET remains very much a plan on paper alone. The ground breaking and signing of MoUs for a railway and pipeline between Kenya, Ethiopia, and South Sudan took place in March 2012 at Lamu. But in a reflection of the long delay of the entire plan, construction of the oil refinery, which was expected to be complete in 2015, had still not begun by mid-2014.[59]

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[51] It will likely have similar design features to the nearly 500-kilometre Mangala Development Pipeline between Rajasthan and Gujarat in India; 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 29.
[52] Zeddy Sambu, 'Government to invite bids for Sh255 billion crude oil pipeline', *Daily* Nation, 8 February 2014, http://mobile.nation.co.ke/business/Government-to-invite-bids-for-Sh255-billion-crude-oil-pipeline/-/1950106/2197832/-/format/xhtml/-/gqgndaz/-/index.html, accessed 28 July 2014.
[53] Yadullah Hussain, 'Canada's Africa Oil Corp. sees promise in Kenya', *Financial Post*, 24 October 2013.
[54] George Mwangi, 'Ecobank: Kenya Oil Segment Needs $16 Billion Investment', *Dow Jones Business News*, 29 July 2014.
[55] Tullow, 'Operational Update – Kenya', Press Release, 15 January 2014.
[56] 'A New Frontier: Oil and Gas in East Africa', *Control Risks*, 2012, 10.
[57] 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 29.
[58] 'Kenya: Lamu – Back to the Future', *African Business Magazine*, 19 February 2012.
[59] 'Emerging East Africa Energy', Energy Information Administration, 23 May 2013.

Oil and construction companies are eager to sign contracts and begin work on LAPSSET. But who pays the bill is still unclear. International investors have not been forthcoming to date, and Kenya's capacity to fund many parts of the massive undertaking is quite limited. Silvester Kasuku, chief executive of LAPSSET, said that the China Communications Construction Company would lead the construction of the nearly $500 million project to build the first three berths of the planned 32-berth port at Lamu,[60] But it took over a year for the Kenyan government to finalize the contract after the Chinese company won the tender.[61]

Figure 9: Regional oil pipeline possibilities

Source: The Economist

The original LAPSSET plan and its huge and diverse infrastructure development goals may need to be significantly downsized to increase viability. A piecemeal approach, beginning with a basic export pipeline and port terminal at Lamu, will likely be the first parts developed. Different consortia have submitted design proposals to construct pipelines within Kenya and between neighbouring Uganda and South Sudan: Tullow/Africa Oil for a Lokichar–Lamu route; Toyota Tsusho for a Hoima (Uganda)–Lamu route; Tullow, Total, and CNOOC for Hoima–Lokichar–Lamu route; LAPSSET for Juba–Lokichar–Moyale–Lamu; and Total for a Hoima–Eldoret–Lamu/Mombasa route.[62] But rather than Kenya joining Ethiopia and South Sudan for export and product pipelines to Lamu, in the short term it is more likely that Uganda and Kenya will establish the first pipeline links with other neighbours joining through oil, road, and rail links in the medium and long term. This in part due to the ongoing civil war and lack of new oil discoveries in South Sudan, as well as unsuccessful exploration in Ethiopia, which deters investors from developing tie-in export pipelines from both countries. Uganda, Rwanda, and

[60] George Mwani, 'Chinese Firm Signs $478.9 Million Kenya Lamu Port Deal', *The Wall Street Journal*, 3 August 2014.
[61] Drazen Jorgic, 'Kenya says Chinese firm wins first tender for Lamu port project', *Reuters,* 11 April 2013.

[62] Zeddy Sambu, 'Kenya amends conditions for pipeline tender following talks with Uganda', *Daily Nation*, 19 July 2014.

Kenya have also signed MoUs on product and export pipelines and may be the first to implement the agreements.[63]

Several of the pipeline plans submitted by international oil companies operating in the region include Mombasa as the end destination for Kenyan and Ugandan crude oil. This may be a more feasible option because an expansion of the otherwise congested Mombasa port is ongoing, there is already product pipeline infrastructure between Mombasa and Nairobi, existing road and rail support is in place to develop new pipelines (unlike the case in Turkana and northern Kenya), and a new Chinese-financed and constructed railway is planned. But LAPSSET holds high political importance for Kenya's government and will not easily be abandoned.

The quality of Ugandan and Kenyan crude is compatible and can flow in the same pipeline, but questions remain over whether the potential Kenya–Uganda oil cooperation will be upended by longstanding competition between the two East African countries. In the words of one international oil company advisor: 'If relations are driven by economics, they will find a solution ... If politics decides, it will be more arbitrary.'[64] If all goes smoothly, the Uganda–Kenya pipeline could be finished by 2019. 'It's not certain, but it's possible,' said the advisor. A transparent regional agreement between Kenya and neighbouring countries, particularly Uganda, and the speedy implementation of such a plan, would help turn rivalries in East Africa into partnerships, and encourage investors. Kenya, which initially did not invite Uganda to participate in regional pipeline plans, has since increased dialogue, and established preliminary agreements with Kampala. But there are still differences that need to be overcome between the East African neighbours.

The cost of a Uganda–Kenya pipeline could be between $2.5 and $5 billion.[65] The exact route will play a large role in dictating the final cost since the requirement that the pipe be heated and insulated increases investment needs substantially. Keeping the pipeline as short as possible is vital for the project's viability. For its part, Uganda is eager to monetize its oil resources, a goal which has been long delayed since its 2006 discoveries. Kampala favours a Southern Corridor, the Hoima–Eldoret–Lamu/Mombasa route, and initially wants to avoid the pipeline link to Turkana.[66] This would establish an independent pipeline system along the existing Nairobi–Mombasa route.

Nairobi, however, is pushing for a Northern Corridor, through Lokichar, and to Lamu in order to develop Turkana's oil resources and meet some of its LAPSSET goals.[67] But the Northern Corridor has a 1,300 kilometre route which crosses over mountainous, isolated, and underdeveloped areas, where rock will need to be removed and roads and supporting infrastructure built, while a three-month rainy season would slow down operations. There would also need to be extensive social engagement with local communities along the route. As a vice president of an international oil company in Kenya said: 'All your communities, all your local authorities, and all your levels of government, along the route of the pipeline will need to be involved'. All these considerations push the costs of the Northern Corridor pipeline to above $4.5 billion.[68]

Kenya's oil resources are still under appraisal by Tullow and Africa Oil, which will help determine whether an East African oil pipeline should first go through Turkana, or a spur line connecting the isolated region to a southern route from Uganda be built later. It will take two to four years to ascertain final commerciality and in the meantime Uganda remains eager to push forward with generating

[63] Sulaiman Kakaire and David Tash Lumu, 'East Africa: Museveni, Kenyatta, Kagame in Ambitious East Africa Devt Plan', *The Observer*, 23 June 2013.

[64] Interview, advisor at international oil company active in East Africa, 26 June 2014.

[65] Drazen Jorgic, 'Kenya attacks undermine plans for east African trade hub', *Reuters*, 20 June 2014.

[66] Interview, vice-president of international oil company active in Kenya, 26 June 2014.

[67] In either the Northern or Southern Corridor, pipeline construction would be spilt into two parts, one beginning from Hoima to the Kenya/Uganda border, the other from the border to Lamu or Mombasa; 'Kenya', Energy Information Agency, Country Analysis Note, April 2014.

[68] Interview, vice-president of international oil company active in Kenya, 26 June 2014.

revenues from its long idle but proven oil reserves. 'Uganda is still the backbone of East Africa oil,' said the international oil company vice president.[69]

Other regional oil infrastructure development plans may act as substitutes for a Kenya-centred regional oil infrastructure network. Oil companies in Uganda are also considering a Uganda–Tanzania route along the west side of Lake Victoria (see Figure 9) instead of through Kenya, but it would need to be far longer than a route through Kenya, and Uganda alone may have to bear the costs.[70] There is competition between Kenya and Tanzania, and their respective ports at Mombasa and Dar es Salaam, and new sites. Kenya is expanding the capacity of the Mombasa port and easing costs for landlocked Uganda and Rwanda in the face of Tanzanian competition.[71] If Kenya wants to maintain its 'Gateway to East Africa' status, it will need to move forward with its infrastructure plans.

Political, social, and security risks

As the oil industry shifts from exploration to development and production, required investments will grow from hundreds of millions to billions of dollars for new oil infrastructure. Tullow Oil, and in particular its smaller and more exploration-orientated partner Africa Oil, will likely sell a share of their interests in the Turkana concessions to larger industry players, such as oil majors and Asian national oil companies, to provide the required capital investments to develop the oil fields. It is at this juncture that risk incentives among the involved oil companies will lower profoundly. During the exploration phase, in the initial drive to discover oil, oil industry operations have been left relatively free from regulatory constraints and political interference. In the upcoming development phase this will likely not be the case. Rather, an 'obsolescing bargain', in which an initial favourable bargaining position for international companies shifts in favour of the government over time, as fixed asset investments increase, may be developing in East Africa.

Political risk

Any business activity is inherently political. This is particularly relevant in a country such as Kenya where politics are so closely tied to business and ethnicity. As a result, the nascent oil industry will not be completely insulated from growing risks in a shifting political and security landscape. The regulatory environment for the oil industry in Kenya is in flux. The planning, establishment, and implementation of a new National Energy Bill and Petroleum Exploration and Development Production Act will have important consequences for the oil industry. New laws will encourage investment on the one hand, particularly in natural gas where there is a lack of regulation, but on the other hand the costs of doing business could increase. And since the political and regulatory environments in Kenya are intertwined, the government may exploit new rules and regulations to advance political and economic goals.

International oil companies have received ample support from both former and current governments in Kenya. International oil companies are confident that the Kenyan government will not delay the start of oil production by stymying foreign investment with restrictive regulations.[72] But the onset of production may very well coincide with political changes in Kenya, as the next general elections are scheduled for August 2017. The incumbent, or a potential new government, may put forward new policies for the oil industry, in an effort to leverage the government's financial position and to gain support from political constituencies, particularly in oil regions and those regions where related infrastructure development is expected. Kenya's mining industry offers examples of how political and

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[69] Interview, vice-president of international oil company active in Kenya, 26 June 2014.
[70] Interviews, senior managers of international oil companies active in Kenya, 26 June 2014 & 9 July 2014.
[71] Sara Jerving, 'Kenya Fights Off Port Competition With $13 Billion Plan: Freight', *Bloomberg*, 20 August 2013.
[72] Interviews, senior managers of international oil companies active in Kenya, 26 June 2014 & 9 July 2014.

legal disputes between local communities and county and central governments can delay commercial activities.[73] Once oil production does begin, and petrodollars flow into government coffers, oil revenue sharing will become a fixture of Kenyan politics.

The Kenyan government is striving to enhance the relatively weak legal and regulatory framework of its 1985 Petroleum Exploration and Production Act. The new law will change the governance structure of the oil industry. To date, the National Fossil Fuels Advisory Committee (NAFFAC), an inter-ministerial body, has been officially in charge of licensing concessions.[74] This power will likely be fully constituted under the Ministry of Energy and Petroleum (MEP) in the new energy policy, while NAFFAC will become a consultation body.[75] The Cabinet Secretary within the MEP will probably maintain the most power in both policy-making and regulatory decisions, leaving space for political interference in the industry.[76] Nonetheless, the 2010 constitution, and the establishment of a National Land Commission in 2012, may have consequences for oil governance in Kenya. It is likely that there will be a multi-tier governance structure over the oil industry, as parliament should be given greater ratification powers over other bodies of government, according to the new constitution.[77] Regulatory responsibility may be shared between national and county governments, as well as various constitutional commissions and government companies and agencies. This presents a complex regulatory landscape for investors to navigate, and may increase the cost of doing business.

There are also a number of specific policy changes in store for the oil industry. Kenya aims to improve its technical capacity to engage and govern the oil and gas sector through the Ministry of Energy and national companies such as: the National Oil Corporation of Kenya, Kenya Petroleum Refineries Limited, and Kenya Pipeline Company Limited.[78] Although the majority of oil concessions have already been licensed out, Kenya has indicated it will introduce bidding rounds in the future to replace direct proposals and the first-come first-served basis under which the industry has operated to date.[79] By mid-2014, the first round was still delayed because the new energy bill had not yet been brought in line with the 2010 constitution and reviewed by parliament.[80] Once competitive bidding does begin, exploration concessions will be expanded from 46 to 51.[81] Future contracts will include new licensing fees, exploration schedules, and requirements to meet annual training fees for Kenyan civil servants. These measures were taken to discourage speculators and encourage exploration and development.[82] Kenya demonstrated the seriousness of its new approach to the industry by its expulsion of Statoil, after the Norwegian company had failed to conduct a 3D survey of its licensed offshore L26 block as demanded by the MEP.[83]

For contract terms, the former Commissioner for Petroleum Energy, Martin Mwaisakenyi, commented that oil companies could recover their costs from exploration, 'cost oil', at 60 per cent per year once production begins. The remaining 'profit oil' will be split between the companies and government depending on production levels: the government share will be 50 per cent up to 30,000 bpd and rise to 78 per cent above 100,000 bpd.[84] The combination of high-cost payments by the government to oil

[73] Steve Mbogo, 'Mui coal plant row goes out of court', *The East African,* 26 October 2013, www.theeastafrican.co.ke/business/Mui-coal-plant-row-goes-out-of-court/-/2560/2047916/-/nc03plz/-/index.html accessed on 10 September 2014.
[74] 'Kenya unveils new oil and gas licensing rules', *The East African*, 15 December 2012.
[75] 'Draft National Energy Policy', Ministry of Energy and Petroleum, Republic of Kenya, 24 February 2014, 22.
[76] 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 31.
[77] 'Kenya', Freshfields Bruckhaus Deringer LLP, March 2013, 2.
[78] 'Second Medium Term Plan 2013–2017', Kenya Vision 2030, Government of the Republic of Kenya, Nairobi, 2013, 69.
[79] 'Kenya Joins East Africa Oil and Gas Frenzy', *Energy Intelligence Finance*, 4 April 2012.
[80] George Obulutsa, 'Kenya delays energy bill until June', *Reuters*, 8 January 2014.
[81] Oil companies will also need to cede 25% of exploration acreage after 2 years onshore and 3 years offshore if work commitments not made; Kennedy Senelwa, 'Kenya set to auction five oil, gas blocks as new rules take effect', *The East African*, 5 January 2013.
[82] 'Kenya unveils new oil and gas licensing rules', *The East African*, 15 December 2012.
[83] Rawlings Otini, 'Kenya expels oil giant Statoil from exploration plan', *Business Daily*, 5 November 2012.
[84] 'Kenya unveils new oil and gas licensing rules', *The East African*, 15 December 2012.

companies and initial low production will result in low initial government profit shares. This may cause some public resentment towards oil companies if expectations of production are not properly managed before it begins.

Kenyan officials have stressed that they do not wish to repeat the delays to oil development witnessed in Uganda. President Kenyatta will likely strive to see oil production as soon as possible in order to capitalize on political credit before the next election, particularly in launching major infrastructure projects to develop the northern and coastal regions where his current support is weak compared to the central counties. But at the same time, Kenyatta does not want to repeat Uganda's negative experience of not capturing significant gains during the development phase of its oil industry. Foreseeing potential large concession interest sales by Tullow Oil and Africa Oil, Kenya plans to impose taxes on oil, gas, and mining companies by the end of 2014, and President Kenyatta says: 'We want to ensure that we as a country also are able to benefit from both the windfall and capital gains tax ... Uganda has lost a lot of revenue as a result of not really having focused on that'.[85]

Unlike the position facing other regional neighbours, there is more potential in Kenya for bottom-up oversight and intervention in the oil industry.[86] In the coming years, Tullow and Africa Oil will need to bring in larger partners to help develop oil resources in Blocks 10BB and 13T of Turkana County. These sales will likely result in public scrutiny of how the two exploration companies acquired the concessions. During the coalition government between 2008 and 2012, high-level politicians allegedly profited from selling oil concessions to international oil companies through private companies (the 2003 Public Officer Ethics Act does not prohibit civil servants from owning stakes or having interests in private companies unless these conflict with official duties).[87] These dealings, together with unfavourable terms for the government in existing contracts, even if they were designed to attract foreign investment to unproven oil regions, may face public backlash and potential review, as has been the case in Ghana, Uganda, and Tanzania in recent years.

Fearing a potential loss of negotiating power, local communities and county governments will also respond to the entry of new oil companies, and may make renewed demands that delay the industry from advancing forward.[88] There is also regional political risk from un-demarcated international borders between Kenya and its neighbours. Somalia is seeking to take Kenya to the International Court of Justice in The Hague over maritime border claims of some offshore concessions.[89] Such disputes may also arise onshore if oil exploration in Turkana County reaches the disputed Ilemi Triangle between Kenya, South Sudan, and Ethiopia.

Social risk

The successful advancement of the 2010 constitution offers potential economic and social development boons and can help reverse high levels of inequality in Kenya. Such a process, however, offers challenges to the oil industry as communities in oil regions and their political representatives grapple with the convergence of new economic resources and increased political power. But a failure by the Kenyan government to successfully implement political devolution could be even more damaging to the timely development of the oil industry. This outcome could see aggrieved counties contest oil resources with the national government and international oil companies. If the objectives of devolution in the new constitution are fulfilled and political power and economic resources shift from the centre to county level, particularly in restless peripheral regions such as Turkana, then conflicts over scarce resources can be mitigated.

[85] 'Blow for Tullow as Kenya eyes windfall tax on oil companies', *The Irish Independent*, 5 August 2014.

[86] David Booth, Brian Coosey, Frederick Golooba-Mutebi, and Karuti Kanyinga, 'East African prospects: An update on the political economy of Kenya, Rwanda, Tanzania, and Uganda', Overseas Development Institute, Report, May 2014, 27.

[87] 'Minister's Firm Sold Turkana Oil Block for Sh800m', *The Daily Nation*, 27 March 2012; Andrea S. Pongo, 'Effects of the 2013 National Elections on Oil Exploration in Kenya', Institute for Defense Analyses, Alexandria VA, 2013, 2

[88] Personal communication, Kenyan academic, 6 September 2014.

[89] 'Somalia takes Kenya to U.N. court in oil rights row', *Reuters*, 29 August 2014.

There has been widespread oil exploration over the past 60 years in Kenya. But to date oil has only been found in Turkana County. Turkana is a large and isolated region located in Kenya's north-west, bordering Uganda, South Sudan, and Ethiopia. Turkana is part of Kenya's arid and semi-arid lands (as are counties within the Anza, Mandera, and Lamu Basins) and it is also one of Kenya's poorest regions, where the vast majority live under the poverty line. As a colonial officer once coarsely (and mistakenly) said of Turkana, it is 'the wildest and most worthless district in Kenya.'[90]

The Turkana population, estimated at over 1 million with a density of two people per square kilometre, is largely pastoralist; the tending of livestock (cattle, sheep, and goats) providing both livelihood and identity.[91] Development in Turkana has been neglected by the central government in Nairobi for decades. It lacks infrastructure, skilled labour, and security, with a large flow of small arms coming through porous borders to and from conflicts in neighbouring countries.[92] Working in such isolated and underdeveloped regions is not uncommon in the international oil industry, but Turkana is nonetheless a difficult and expensive operational environment.

The national–local political divides, local competition, and the possible and perceived environmental impact of the oil industry have all fuelled concerns that Turkana may take on some of the negative traits of poverty and conflict associated with oil development in Nigeria's Niger Delta. Sparking superstitious concern, rig 804 operating at the Ngamia 1 well (the site of Kenya's first oil discovery) was previously used in the Niger Delta.[93] But the situation in Turkana is a long way off such environmental degradation and armed conflict. And Kenya's relatively strong civil society, media, and judicial system can act to prevent these traits from developing, if mechanisms to settle political and social grievances are conceived.

In Turkana, expectations are high that oil will bring fast-paced economic growth and development. Managing these expectations according to both the long timeframe for oil development and the limitations of what are still relatively small oil discoveries, is regarded as one of the main challenges facing the Kenyan government and international oil companies in relations with local communities.[94] As a senior manager at Africa Oil said: 'The oil and gas industry cannot be the game changer in the country's north ... At best, it can be a stimulus'.[95] There is also apprehension among the local population that they will be left out of the oil boom. In this sense, oil companies will be well advised to manage their expectations of time constraints on operations, and the importance of relations with local communities, in the social and political environment in which they are working.

Speaking at a meeting on the sidelines of the US-African Leaders Summit in Washington DC in August 2014, President Kenyatta underlined his willingness to make oil contracts publicly available.[96] Although the Kenyan president's position may be geared towards attracting further US investment to Kenya's oil sector, Kenyatta visited Houston and potential investors, including ExxonMobil and

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[90] Rayner, H., *The Ivory Traders*, London: W. Heinemann, 1923, quoted in R. Dyson-Hudson and J. Terrence McCabe, *South Turkana Nomadism: Coping with an Unpredictably Varying Environment*, Ethnography Series, FLI7-001. New Haven: HRAFlex Books, 1985.

[91] Eliza M. Johannes, Leo C. Zulu, and Ezekiel Kalipeni, 'Oil discovery in Turkana County, Kenya: a source of conflict or development?', *African Geographical* Review, 2014, 3–5.

[92] Patricia I. Vasquez, 'Kenya at a crossroads: Hopes and fears concerning the development of oil and gas reserves', *Articles and Debates*, 4.3, International Development Policy, Graduate Institute of International and Development Studies, 2013, 7.

[93] 'Kenya oil: Inside Tullow Oil Ngamia 1 rig in Turkana', *Kenya Reporter*, 12 April 2012.

[94] Ryan Cummings, 'Predicting Africa's Next Oil Insurgency: The Precarious Case of Kenya's Turkana County', *Think Africa Press*, 13 September 2013, http://thinkafricapress.com/kenya/predicting-next-oil-insurgency-precarious-case-turkana-county accessed 14 August 2014.

[95] 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 68.

[96] Ian Gary, '"Absolutely" – Kenya President backs full oil contract disclosure', *The Politics of Poverty*, 27 August 2014, http://politicsofpoverty.oxfamamerica.org/2014/08/absolutely-kenya-president-backs-full-oil-contract-disclosure/ accessed 11 September 2014.

Conoco Philips,[97] Tullow and other oil companies present in Kenya are supportive of publishing the contracts and environmental impact assessments.[98] The draft of the National Energy Policy calls for 20 per cent of 'the government share of profits from energy natural resources' to be shared with the county government and 5 per cent with the local community (determined by the sub-county where the resource exists and delivered by the county government).[99] These are all positive indications, but have not yet been followed through with action. If the central government does not manage the oil industry in a relatively transparent manner, then the obscure distribution, budgeting, and expenditure of oil revenues will create further grievances among local populations.

Just as political tensions are present around oil at the national–local level, they also exist between local communities and their political representatives, together with wrangling between the governor, MPs, and the senate. The lack of capacity, in county governments and local communities, to assess the social and environmental impact of the oil industry, to negotiate business involvement, and to manage possible future revenues, has created concern that governance flaws in Kenya will simply be relocated from the central to the county level through political devolution.[100] How the county level government disseminates its oil revenue share is critical. Local communities not in the sub-counties where oil is produced, but nonetheless affected by oil operations and infrastructure, may make strong demands for revenue shares. Oil companies may become conduits for local communities to attempt to amend social grievances with local and national government and be scrutinized for their own behaviour in a regulatory weak business environment.

Even though still in the exploration and development phase, social grievances among the local population have constrained oil operations in Turkana. In late October 2013, Tullow suspended its operations in Block 10BB and 13T in Turkana in the face of demonstrations by hundreds of local residents over the lack of employment and business opportunities. The respective members of parliament in Turkana South and Turkana East led local residents in the protests. They marched on the Twiga 1, Etuko, and Ngamia 1 oil well sites and shut down operations in the two districts for several weeks in the process.[101] While the local MPs were detained and questioned for a period by Kenya's Police Criminal Investigation Department,[102] the central government sent representatives to meet with community leaders to defuse the situation. There were wide-reaching consequences for international oil companies involved in the concessions. Stock of Tullow Oil and its partner Africa Oil dropped by 1.4 per cent and 2 per cent respectively upon the news.

Tullow responded to these grievances through a Memorandum of Understanding (MoU) that underlined the company's commitment to using local staff, goods, and services (even before the incident over half of its 1,400 staff in Kenya came from Turkana), pledged to agree on a formal grievance resolution procedure, committed to doubling its social investments in 2014 to $2 million (from $1 million in 2013), and opened community resource offices in Lodwar, Lokori, and Lokichar.[103]

[97] Samuel Kamau Mbote, 'President Kenyatta to visit Texas for energy related discussions', *Oil News Kenya*, 8 August 2014, http://oilnewskenya.com/2014/08/08/president-kenyatta-to-visit-texas-for-energy-related-discussions/ accessed 28 September 2014

[98] Personal communication, representative of international oil company active in Kenya, 7 September 2014.

[99] 'Draft National Energy Policy', Ministry of Energy and Petroleum, Republic of Kenya, 24 February 2014, 130 & 146.

[100] Patricia I. Vasquez, 'Kenya at a crossroads: Hopes and fears concerning the development of oil and gas reserves', *Articles and Debates*, 4.3, International Development Policy, Graduate Institute of International and Development Studies, 2013, 7.

[101] Lucas Ngaasike, 'Tullow Oil suspends operations over conflict with locals', *The Standard*, 28 October 2013.

[102] Cyrus Ombati and Lucas Ng'Asike, 'MPs grilled over protests at Tullow Oil well, Turkana', *The Standard*, 30 October 2013, www.standardmedia.co.ke/thecounties/article/2000096529/mps-grilled-over-protests-at-tullow-oil-well-turkana accessed 14 August 2014.

[103] Michael Kavanagh and Katrina Manson, 'Tullow temporarily halts Kenya work after protests, *Financial Times*, 28 October 2013; 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 53; 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 27.

But since there is little oversight over the MoU, which excluded consultations with civil society in its drafting, it may be only a temporary fix.[104]

The protest was a product of the desire of the Turkana people themselves, rather than 'foreigners', to benefit from oil specifically (from the perspective of most Turkana people, other Kenyans who do not come from the region are also regarded as foreigners).[105] It was also the result of infighting among the Turkana people. Oil has been confirmed in South Turkana, and people in the sub-county want to see the majority of the jobs, contracts, and other boons from oil development come their way first before they spread to others in the county.

There are also acute concerns among local residents that their political representatives will exploit their positions to advance their own interests in collaboration with oil companies.[106] In June 2012, in Lodwar, the capital of Turkana County, community leaders claimed local officials had exploited their positions to profit from land acquisitions by the oil industry and had intimidated and displaced communities near oil wells. Tullow was accused by local communities of colluding with county and national officials in not publishing environmental impact assessments, not compensating local communities sufficiently, bribing local officials to secure land, not employing enough local people, and not providing adequate compensation for claims of losses incurred from oil exploration activities.[107]

Local content will be a critical political and social issue for oil operations in Kenya. The national government wants to leverage Kenyan companies' activities and provision of goods and services in the oil industry.[108] But local content cannot be easily separated from often-divisive politics in Kenya and close links between business and political interests. International oil companies will be hard pressed to navigate, at times, competing interests between the national government, county governors, MPs, the county senate, and local communities.[109] Tullow has been increasingly transparent about its payments to Kenyan stakeholders. In 2013, it spent $71 million altogether on local suppliers, taxes, and community development.[110] But as investment levels rise during the development phase, oil companies will be expected to increase their engagement with Kenyan companies, labour, and investments in local communities. Since there is a limit to engagement with local communities in Turkana, due to their lack of skills and capacity to work in the oil industry, tensions between the national and local level should be expected as other Kenyan companies and non-Turkana labour move in to fill the vacuum, until the Turkana people can play a deeper role in the oil industry through training.

In Turkana, where arable land and water are scarce, acute environmental concerns are attached to the expansion of the oil industry. Kenya's National Environment Management Authority (NEMA) is charged with monitoring compliance to environmental and social safeguards, but is understaffed and underfunded.[111] NEMA may muster its resources to focus on big industries and projects, such as oil

[104] 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 54.
[105] Personal communications, Kenyan academic. 9 September 2014.
[106] 'Governor Nanok clarifies why Turkana county returned Sh3b to National treasury', *The Standard*, https://www.standardmedia.co.ke/campus/story/2000133442/governor-nanok-clarifies-why-turkana-county-returned-sh3b-to-national-treasury, 1 September 2014, accessed 10 September 2014; Personal communications, Kenyan academic. 9 September 2014.
[107] Ryan Cummings, 'Predicting Africa's Next Oil Insurgency: The Precarious Case of Kenya's Turkana County', *Think Africa Press*, 13 September 2013, http://thinkafricapress.com/kenya/predicting-next-oil-insurgency-precarious-case-turkana-county accessed 14 August 2014; Personal communication, Kenyan academic, 6 August 2014.
[108] 'Kenya', Freshfields Bruckhaus Deringer LLP, March 2013, 4.
[109] 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 69.
[110] In 2011, Tullow spent $23.6 million on local suppliers. This represented 23% of its overall spending in Kenya, 'Kenya unveils new oil and gas licensing rules', *The East African*, 15 December 2012; 'Tullow Oil, Annual Report 2013', Tullow Oil, London, 2014, 24.
[111] Patricia I. Vasquez, 'Kenya at a crossroads: Hopes and fears concerning the development of oil and gas reserves', *Articles and Debates*, 4.3, International Development Policy, Graduate Institute of International and Development Studies, 2013, 7.

and gas, but there are also allegations that it is fraught with corruption.[112] Since enforcement can be lacking, some self-regulation may be required by the oil industry if a regulatory vacuum continues.

The struggle over scarce resources in Turkana is spilling over into oil. After the discovery of oil at Ngamia 1 by Tullow Oil, the Turkana and Pokot (a neighbouring ethnic group) disputed the location of the well; the Pokot accused the Turkana of illegally occupying the land.[113] The Turkana–Pokot oil dispute threatens to serve as a new frontier of a traditional rivalry over cattle, water, and pastures.[114] Too often international oil companies have described such local disputes and armed fighting as 'occasional intertribal conflict' to assuage investor concerns.[115] But when these are actually decades-old conflicts,[116] it does not serve the interests of companies to downplay their existence. While Tullow, Total, and BG Group are signatories to the Voluntary Principles on Security and Human Rights (a set of human rights guidelines for extractive industry companies) some capacity to deal with insecurity in a manner compatible with international best practice is required within the Kenyan security forces.[117]

The demands for more benefits from the oil industry are not necessarily just a product of overblown expectations among local communities, they are also a result of witnessing the damage that oil development has caused in the past in Kenya and elsewhere in Africa. Local communities are not unaccustomed to dealing with oil companies. Oil exploration has gone on for some six decades across large swaths of Kenya, and not without negative experiences for local communities. Some communities have accused oil companies once operating in the country of harming livestock, after waste was dumped.[118] For example, in Marsabit County locals claim that waste dumped in abandoned oil wells is the source of increased incidences of cancer and other chronic ailments among humans and livestock.[119]

Employment issues are also hotly contested at the local level and have a history that predates oil. The Kenyan government and NGOs and international organizations have been the largest employers in Turkana to date, but nonlocal Kenyans hold the majority of the jobs.[120] Although largely lacking the skills and education to participate, the uneven distribution of jobs has nonetheless created discontent among the Turkana; this, as a result, has amplified recent hostility towards the oil industry regarding hiring practices. These negative experiences fuel mistrust towards current operators.

The Swedish firm, Lundin, claims that before it arrived in 2007 no oil company had ever taken a systematic approach to community engagement.[121] Many exploration companies have shorter time horizons and little capacity to engage in community development programmes. Local politicians and communities in Turkana remain fearful that Tullow, which has made significant discoveries, will exit after selling these resources to new companies, while local communities will have to renegotiate conditions with new companies, losing any commitments and benefits they negotiated with the current companies.[122] While Tullow is increasingly involved in production activities around the world, and will most likely keep a significant share in its Kenyan concessions, other more exploration-focused companies may seek early monetization of their interests.

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[112] *Brian Otieno,* 'Two NEMA Officials Probed Over Graft', *The Star*, 8 February 2014.
[113] Patricia I. Vasquez, 'Kenya at a crossroads: Hopes and fears concerning the development of oil and gas reserves', *Articles and Debates*, 4.3, International Development Policy, Graduate Institute of International and Development Studies, 2013, 7.
[114] Personal communication, Kenyan academic, 6 August 2014.
[115] Christine Batruch, 'Lundin Petroleum AB's experience in East Africa: the role of the private sector in conflict-prone Countries', *The Economics of Peace and Security Journal*, Vol. 5, No. 2,2010, 7.
[116] Eliza M. Johannes, Leo C. Zulu, and Ezekiel Kalipeni, 'Oil discovery in Turkana County, Kenya: a source of conflict or development?', *African Geographical* Review, 2014, 7.
[117] Personal communication, representative of international oil company active in Kenya, 7 September 2014.
[118] Christine Batruch, 'Lundin Petroleum AB's experience in East Africa: the role of the private sector in conflict-prone Countries', *The Economics of Peace and Security Journal*, Vol. 5, No. 2, 2010, 9.
[119] Personal communication, Kenyan academic, 6 August 2014.
[120] Eliza M. Johannes, Leo C. Zulu, and Ezekiel Kalipeni, 'Oil discovery in Turkana County, Kenya: a source of conflict or development?', *African Geographical* Review, 2014, 11.
[121] Christine Batruch, 'Lundin Petroleum AB's experience in East Africa: the role of the private sector in conflict-prone Countries', *The Economics of Peace and Security Journal*, Vol. 5, No. 2, 2010, 7.
[122] Personal communication, Kenyan academic, 6 August 2014.

The implementation of new legislation may be the answer to settling community concerns on concession sales. The possible retrospective effect of new laws coming out of Kenya's 2010 constitution – such as the Community Land Bill – may at first glance appear to upset oil industry interests,[123] but opposition to the advancement of such laws may actually backfire if the alternative is a hostile operational climate. If these social grievances go unaddressed then the operations of the oil industry will be delayed and limited due to protests, blockages, sabotage, theft, and even armed attacks.

Security risk

Not only is the starting point of Kenya's oil production under threat from political instability and insecurity, but also its exit to international markets on the coast. Kenya's coastal communities have longstanding social and political grievances with the central government in Nairobi. Internal politics alone have the capacity to create insecurity for the oil industry if planned pipeline and other downstream infrastructure is targeted. But there is also the possibility that these disputes could become a toxic mix with the incursion of the Somalia-based militant group al-Shabaab on the coast – delaying and hampering large-scale investments in the process.

Al-Shabaab may be positioning itself to exploit social and political tensions to win support from local populations on Kenya's coast. But if the Kenyan government is able to advance political devolution to coastal counties, while working to contain al-Shabaab in an apolitical manner, then there is a strong likelihood that, with regional and international support, Nairobi will be able to curb the militant group's activities, allowing the oil industry to operate in a relatively secure environment. If Kenya is to become the transit hub for East Africa's oil boom, and fend off competition from Tanzania, then relative stability and security on the coast must be achieved.

The coastal regions, similar to Turkana, are some of the least developed in Kenya. There exist severe social grievances over neglect by the central government in Nairobi, particularly among the Muslim population. This is coupled with feelings of exploitation over land rights (since Kikuyu settlers came to the region in the 1960s) and the incursion of Kenyan companies from the Nairobi area into the coast's prosperous tourism sector. These grievances have fuelled separatist sentiment through groups, such as the Mombasa Republican Council (MRC) whose common slogan is *Pwani Si Kenya* or 'The Coast is not Kenya'.

At the same time, a series of terrorist attacks carried out by al-Shabaab over the past two years has heightened security concerns in Kenya. The militant group claims that such attacks are in response to Kenya's military incursion, first unilaterally and then through the African Union force in southern Somalia in 2011. In September 2013, 67 people were killed in a dramatic terrorist attack on the Westgate Shopping Mall in Nairobi. A bomb attack killed 10 people in the capital in May 2014. Later, following five attacks connected to al-Shabaab on coastal communities in Lamu and Tana River counties, over 100 were left dead (Mombasa County had been targeted in earlier attacks). The insecurity has negatively affected tourism, as the USA, Britain, and other western governments have issued travel advisories.[124] A security response from the Kenyan government may be necessary to dissuade attacks in the near future, but a long-term solution to contain al-Shabaab requires a political settlement, which must include some degree of stability in Somalia.[125]

The threat posed by al-Shabaab to the oil industry should not be over amplified. But there is growing concern that terrorist attacks in Kenya over the past few years may widen political divides between Nairobi and the coast. The targeting of, and discrimination shown against, Kenyan Somalis and

[123] Harold Ayodo, 'Tullow Oil's move on land Bill opposed', *The Standard*, 24 April 2014.
[124] Jeffrey Gettleman, 'Gruesome Attacks in Kenyan Villages Heighten Fears of a Nation on Edge', *The New York Times*, 7 July 2014.
[125] 'Somalia: Al-Shabaab – It Will Be a Long War', *International Crisis Group*, Africa Briefing No 99, 26 June 2014.

Muslims by Kenyan security forces in the wake of the Westgate attack provides recruitment possibilities and avenues of support for al-Shabaab in Kenya.[126] After the terrorist attacks on coastal villages, in which the many of the victims were Kikuyu (Kenya's dominant ethnic group, and that of President Kenyatta) security authorities and the president himself linked the killings to local political groups such as the MRC.[127] In a statement on 17 June, Uhuru Kenyatta said: 'The attack in Lamu was well planned, orchestrated, and politically motivated ethnic violence against a Kenyan community, with the intention of profiling and evicting them for political reasons'.[128]

Some observers believe that al-Shabaab is deliberately trying to undermine political stability in Kenya through targeted attacks on Kikuyus in coastal regions.[129] Although he later advanced the theory that al-Shabaab may have played a role, President Kenyatta's politicization of the attacks sparked concern that the security situation may worsen because internal divisions between ethnic groups had been enflamed.[130] Such tensions are aggravated when rich Kenyan speculators from Nairobi and the Rift Valley buy up acreage in Lamu County, with intentions of later selling the land when schemes for government-planned infrastructure increase prices.[131] Possibly in an attempt to subdue some of these concerns, President Kenyatta recently ordered the repossession of 500,000 acres of public land after an audit found developers had acquired ownership under 'dubious and suspicious corrupt circumstances'.[132]

The consequences for the oil industry of the insecurity on Kenya's coast are already starting to show. One oil company assigned a 'business critical' status to travel to Nairobi in the wake of terrorist attacks.[133] Other exploration activity, in Blocks 3A and 3B in northern Kenya near the border with Somalia, has been delayed, due in part to security concerns.[134] 'Al-Shabaab is target oriented and pretty mobile', said one advisor at an international oil company active in Kenya.[135] The ability of Kenya's Defence Forces, National Intelligence Service, and National Police Service to protect critical infrastructure in the energy sector has also come under question, on account of the lack of a key authority covering security measures and competition between government ministries on security issues that would foster information sharing, which is otherwise inhibited.[136]

Security concerns will entail extra insurance premiums for the financing of a possible Uganda–Kenya pipeline, pushing its cost to the higher end of the $2.5 to $5 billion estimate.[137] Tullow has suggested that any consortium of companies building a pipeline will need to bury it underground for security and environmental reasons, following international best practice in the industry. This would increase construction time, but in the long run, a buried pipeline would help avoid the oil bunkering witnessed in Nigeria and have a smaller footprint on pastoral livelihoods in Kenya's north.[138]

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[126] 'Kenya and its coastal discontents', *Aljazeera*, 26 September 2012, www.aljazeera.com/indepth/opinion/2012/09/20129238293700321.html accessed 14 August 2014.

[127] Robyn Dixon, 'Tension rises in Kenya as 29 are killed in attacks on coastal towns', *The Los Angeles Times*, 6 July 2014.

[128] 'Conflict dynamics on Kenya's coast', *IRIN*, 23 July 2014, www.irinnews.org/report/100394/analysis-conflict-dynamics-on-kenya-s-coast accessed 14 August 2014.

[129] Mohamed Mubarak, 'Al-Shabaab's foreign operations arm is busy recruiting in Kenya', *African Arguments*, 3 July 2014, http://africanarguments.org/2014/07/03/al-shabaabs-foreign-operations-arm-is-busy-recruiting-in-kenya-by-mohamed-mubarak/ accessed 14 August 2014.

[130] Murithi Mutiga, 'Al-Shabaab Lays a Trap for Kenya', *The New York Times*, 29 June 2014.

[131] 'Lapsset, oil discovery triggers real estate boom in Lamu Archipengo', *The Standard*, 21 May 2014.

[132] 'Kenya's leader Kenyatta orders Lamu land repossession', *BBC News*, 1 August 2014.

[133] Magnus Taylor, 'Kenyan gloom and ineffective authoritarianism: free-form thinking on the state of Eastern Africa', *African Arguments*, 7 July 2014, http://africanarguments.org/2014/07/07/kenyan-gloom-and-ineffective-authoritarianism-free-form-thinking-on-the-state-of-eastern-africa-by-magnus-taylor/ accessed 14 August 2014.

[134] 'Setting the Agenda for the Development of Kenya's Oil and Gas Resources – The Perspectives of Civil Society', The Kenya Civil Society Platform on Oil and Gas (KCSPOG), Nairobi, July 2014, 10.

[135] Interview, 26 June 2014.

[136] E.O.S Odhiambo, T.L Maito, and K. Onkware, 'Kenya's oil pipeline and terrorism', *Journal of Defense Resources Management*, Vol. 5, Issue 1, 2014, 27–8.

[137] Drazen Jorgic, 'Kenya attacks undermine plans for east African trade hub', *Reuters*, 20 June 2014.

[138] Personal communication, representative of international oil company active in Kenya, 7 September 2014.

Reform in Kenya's security establishment and ongoing cooperation with the USA may serve to curtail attacks against infrastructure and weaken al-Shabaab.[139] International oil companies are also not unaccustomed to operating in insecure environments. While there has been no serious attack against oil installations in Kenya to date, investors are still concerned that ongoing insecurity along the coast will delay planned infrastructure projects, increase costs, and prolong construction time. In particular, if insecurity persists, the Kenyan government's ability to obtain financing for the ambitious $25 billion LAPSSET port and transport infrastructure project will be limited.

Conclusion

It is still early days for oil development in Kenya. Opportunities for new oil and gas exploration are many, but it is far from certain that significant new discoveries will be made. Expectations of what oil can bring for economic growth and development are far ahead of the level of actual discoveries to date. Even if Kenya's oil resources of 600 million barrels were to multiply with new finds in the coming years, the country would still only be able to play the role of a small African producer. Kenya's role as a regional transit hub for East African oil and gas, however, could prove to be more significant.

Politics will weigh heavily on the oil industry in Kenya, regardless of how large it becomes. The favourable business environment for international oil companies is shifting towards greater regulation and the potential for higher levels of political interference. With the August 2017 general election on the horizon, either the incumbent or a new government could exploit new rules and regulations to put forward political and economic goals.

At the same time, the 2010 constitution promise of a decentralization of political and economic decision-making power from the central government in Nairobi to 47 new counties is still underway. Counties are coming to terms with the convergence of new economic resources and increased political power through devolution. Oil has already become a point of contention between the national and local level in Turkana County and has caused rifts between county political representatives and local communities. Disputes will continue to stall progress in the oil industry, until the different levels of government in cooperation with international oil companies and local communities develop formal mechanisms to settle these grievances.

Finally, security concerns loom as the oil industry strives to move from the exploration to the development phase. Already hostile relations between the central government and coastal and north-eastern counties could slow down or upend plans for large oil infrastructure. The incursions of al-Shabaab in Kenya threaten to add fuel to these long-standing animosities, but the advancement of the new constitution could help mitigate insecurity. Kenya could very well develop both into Africa's newest oil producer and the regional centre for oil and gas transit by the end of the decade.

[139] In September 2014, a US armed drone targeted and reportedly killed the al-Shabaab leader, Ahmed Abdi Aw Muhammad, commonly known as Godane; Stig Jarle Hansen, 'How will the death of its leader, Ahmed Godane, impact Al Shabaab?', *African Arguments*, 8 September 2014, http://africanarguments.org/2014/09/08/how-will-the-death-of-its-leader-ahmed-godane-impact-al-shabaab-by-stig-jarle-hansen/ accessed 12 September 2014.