Flagler Expro Argentina Requests New Capital

A Case Study in Parent vs. Affiliate Project Economics in a Risky Location

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Abstract

Economics for international energy projects differ from those developed for home country projects. For one thing, international projects usually involve different currencies. These must be translated back to the home currency. $US prices may pertain to some revenues/costs and not others. Local taxes are usually different, and have to be integrated into the firm's overall tax position. The biggest changes, however, pertain to risky locations. There investors need to worry about such outsized risks as currency maxi-devaluations, inconvertibility, wholesale tax regime changes and expropriation. The format for project economics must then change to accommodate projections for these issues. This case considers an investment opportunity in such a risky location. Argentina has inflicted all of the above-mentioned events on investors in the past. How should Flagler reflect these concerns as it considers Expro Argentina's request for new capital?

The case provides students with a capital Appropriation Request (See Attachment 1) typical of what affiliates submit to headquarters. The buyout opportunity appears attractive. Annex 1 contains project assumptions and economics, and shows a 16% IRR.

Do the affiliate economics include all factors germane to the parent's decision? Are all the tax and corporate network effects included? Will $US oil prices continue to determine revenues? Are Argentina's investment risks adequately reflected from the parent's perspective? Attachments 2 and 3 provide the parent company's templates for adjusting affiliate economics. Students must decide which to use and how to reflect the specifics of Expro Argentina's situation. Will the Bridas buyout still be attractive on this "parent adjusted" basis?

Like all forecasts, project economics are likely to be inaccurate. They can, however, be immensely useful for provoking examination of the right issues. In this case, properly framing Argentina's risks can lead Flagler to consider a wide range of options, including obtaining political risk insurance, employing project finance, borrowing local funds and deferring any buyout offer until after certain events have transpired.