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Countdown begins for $10bn Pluto project

Woodside Petroleum Ltd is fast approaching decision time on its giant Pluto gas project, which, if it proceeds, will be the single largest investment in a resource project in Australia's history. Mark Beyer reports.

ENERGY DECISIONS

- Pluto LNG project likely to cost up to $10bn.
- This is four times the cost of NW Shelf venture's Phase 5 expansion
- Woodside board decision due mid 2007.
- Sunrise LNG project tipped to follow in the next three years.
- Browse Basin development, costing up to $20bn, looking doubtful.

SPECIAL REPORT

MICHAEL Chaney made many big investment decisions when he ran Perth's biggest industrial company, Wesfarmers Ltd, but nothing compares with the decision Woodside Petroleum's board of directors will consider as early as this month.

As Woodside's chairman-elect, Mr Chaney will play a key role when the board decides whether to press the button on the giant Pluto LNG project, estimated to cost up to $10 billion.

If Pluto proceeds, it will be the first big LNG project to get under way anywhere in the world in nearly 18 months.

Pluto has the potential to transform Woodside and it's not the only big issue facing Western Australia's largest resources company.

With costs rising rapidly, Woodside is reviewing some of its far-flung operations, in places such as Mauritania and onshore Libya, to focus more on its core operations.

It is also looking beyond Pluto, with industry analysts tipping that its next big move will be development of the Sunrise project in the Timor Sea.

The big winners from Sunrise are likely to include the Northern Territory, since the LNG is likely to be processed in Darwin.

That means Woodside's much

larger, and more challenging Browse Basin project, off the coast of Broome, is expected to slip back in the development queue.

Ironically, the issue that has attracted more news coverage than any other – the controversy over the state government's domestic gas reservation policy – is considered a non-issue by analysts who follow Woodside.

The Pluto project has progressed remarkably quickly, in contrast to many other big LNG opportunities around the globe that have been deferred because of political risks, environmental concerns and rapidly increasing costs.

A prime example is Chevron's Gorgon project, which is still awaiting final environmental approvals from the state government.

The Pluto project has faced its share of hurdles, not the least of which is the cost pressures that affect Woodside as much as every other major project developer.

Woodside has also had to deal with question marks over the size of the Pluto resource, which is small by international standards, and concern over rock art on the Burrup Peninsula, where the LNG plant is to be built.

Despite all this, analysts are confident Pluto will be approved when the board considers a final investment decision (FID).

"FID is planned for mid 2007 and we continue to believe this is likely especially since the board has already approved expenditure of up to $1.4 billion for long-lead items and site works," Goldman Sachs JBWere analyst Anthony Bishop said in a recent research note.

JPMorgan analyst Mark Greenwood was more forthright, saying there was little doubt that the Pluto project would be approved, probably at Woodside's August board meeting.

Woodside managing director Don Voelte has championed the Pluto project.

"Pluto is on track to become the world's fastest LNG project from discovery to production," he told the annual general meeting two months ago.

Woodside discovered the Pluto gas field in April 2005 and just four month later announced it was considering development of the field.

Initially, it aimed for an LNG plant with annual output of between five million and seven million tonnes, and said capital spending was likely to involve "several billion dollars".

It subsequently said the cost would be in a range of $6 billion to $10 billion.

JPMorgan's Mr Greenwood estimates the capital spending will be towards the top end of the range, at $9.3 billion, while output is likely to be at the bottom end of the range, at 5mt.

The contrast with the current expansion of the North West Shelf Venture's LNG plant – in which Woodside is the operator and a one-sixth owner – is stark.

The NWS Venture is spending $2.4 billion on the phase 5 expansion, which includes construction of an LNG processing train with annual capacity of 4.2mt and associated infrastructure including a second loading berth.

In other words, Pluto on its own will cost four times more than the phase 5 expansion, yet Pluto's output will be only 20 per cent higher.

That begs an obvious question: why not fold the Pluto project into the NWS Venture and add a sixth train to the existing LNG plant?

A Woodside spokesman said the company and the NWS Venture have held discussions in the past but have not been able to reach a commercial agreement over Pluto.

WA Business News has been told that the NWS Venture is planning to have one more attempt to gain control of Pluto by making a pitch direct to the Woodside board.

Woodside has argued previously that its 100 per cent ownership of

Pluto allowed it to be nimble and decisive, so that first production could be achieved by 2010.

This would allow the company to exploit a window of opportunity in the global LNG market between 2010 and 2012.

However, chairman Charles Goode told the annual meeting the LNG market had changed in the past year, with the company seeing "a rapid escalation in the price being negotiated for new long-term LNG sales into Asia".

Mr Goode said LNG buyers in the Asia Pacific were looking favourably at Australia as a supplier.

"The need for portfolio diversity and supply security mean that Australian projects are the customers' first choice for new supplies," Mr Goode said.

"It is our view that our projects will no longer be held up by the need to capture markets." What will hold up its projects is the limited ability of industry to build and deliver the LNG plants.

"Due to limitations of skill resources, contractors and capital capacity, we will need to sequence our projects after our first Pluto train," Mr Voelte told the annual meeting. Against this backdrop, the upside for Woodside in going alone on Pluto is that it will not have to share the expected revenue and profits with its joint venture partners (though it has agreed to sell a 5 per cent stake to its two anchor customers).

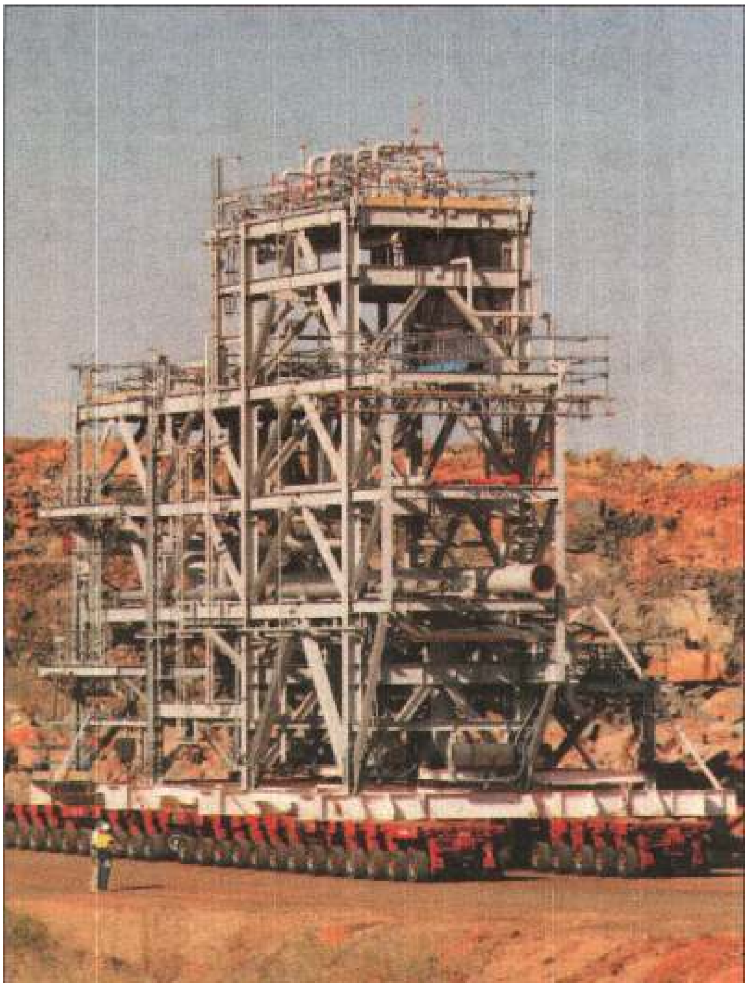
As Mr Goode told the annual meeting, Woodside's share of LNG output was just over 1mt in 2003, and this was expected to double by the end of 2008.

"Over the next decade, we believe we can achieve another five-fold increase, positioning Woodside as one of the world's major suppliers of LNG," Mr Goode said.

Woodside has several big growth opportunities ahead.

It could expand the Pluto LNG project with the addition of a second or third production train, lifting total LNG capacity to as much as 12mt.

The company believes its Browse Basin project, located off the coast of Broome, could support two LNG production trains with capacity of up to 15mt.



PLUTO PLAN: Woodside Petroleum is managing the expansion of the North West Shelf venture's LNG plant on the Burrup peninsula, which has been earmarked for its planned Pluto LNG plant. ***Photo:* Courtesy Woodside**

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It is also pursuing the Sunrise project in the Timor Sea, following the settlement of legal and regulatory issues between Australian and East Timor.

Industry analysts have generally assumed that Browse would follow the Pluto development, in part because of the legal uncertainty that had been hanging over the Timor Sea.

However, Mr Greenwood takes a different view.

"The most attractive project in Woodside's LNG portfolio in our view is the Sunrise project," he said.

The reservoir is fully appraised, has high liquid content, minimal carbon dioxide and would most likely be a brownfields project at the Bayu Undan LNG plant at Darwin, Mr Greenwod said.

He said Sunrise could proceed in the next three years, subject to agreement with the government of East Timor.

In contrast, he said Browse was the most commercially significant project but the most technically and environmentally challenging.

He estimates Browse could cost $21 billion to develop, and he suspects that achieving alignment between the joint venture partners may be difficult.

Mr Greenwood said first production in 2014 was the best-case scenario for Browse.

When valuing Woodside, Mr Greenwood factors in "100 per cent of our Pluto valuation, 60 per cent of Sunrise and 40 per cent of Browse given our level of confidence of each project proceeding".

He does not factor in any value for expansion of the Pluto LNG project, even though the company has talked about the possible development of a second or third LNG train.

"It is not appropriate to factor in value for this at this stage given that additional (gas) discoveries are first likely to extend the reserve life of the first Pluto LNG train," Mr Greenwood said.

Don Voelte