PNG Chamber of Mines and Petroleum

Helping Papua New Guinea to Develop its Full Potential

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Executive Director writes...

The sudden plunge in oil and gas prices worldwide is generating concern about the medium term outlook for oil exploration and development in PNG with most global producing companies sharply curtailing exploration programs and capital expenditures.

In the short term, PNG is fortunate that a number of commitments are at a stage where they are moving ahead expeditiously. This includes extensive exploration programs in Gulf Province undertaken by InterOil, additional drilling at Hides and Angore by the PNG LNG Project and the likelihood of two wildcat wells in the Madang-Ramu area by newcomer Heritage Oil.

With crude oil prices having fallen by 60% from peak levels last year to around US$50 a barrel, all companies are reassessing their exploration programs particularly in high cost environments. Oil Search recently reported its Kutubu Blend price had fallen by 27% to US$73.64 a barrel in the December quarter.

Many analysts and commentators are suggesting that oil prices could remain depressed for up to 12 to 18 months in the face of excess global supplies as well as slowing demand in a number of countries, including China.

While most analysts are anticipating reduced output from higher cost shale oil and other unconventional oil production in the United States and elsewhere, there are signs of a possible slowdown in the LNG sector as well.

The big Royal Dutch Shell Group has announced the cancellation of its well advanced LNG project at Gladstone in Queensland with its partner, Arrow Ltd. They expect to divert methane production from Queensland's coal fields to other Gladstone-based LNG exporters.

Because of high development costs, it is doubtful that most companies would commit to new LNG projects as long as the crude oil price remains around US$50 a barrel (LNG prices are linked to crude oil prices). Many commentators are hopeful prices could rise to US$70 by the end of this year.

A sustained fall in the oil price is likely to see exploration activity in PNG badly impacted, as has already been the case for mineral exploration.

INDUSTRY NEWS - PETROLEUM

PNG LNG Project Enjoyed Full Production in December Quarter

The PNG LNG Project enjoyed its first full quarter of production in the December quarter with commencement of all four long-term LNG contracts in Japan, China and Taiwan, according to Oil Search Ltd.

In its latest December quarterly, Oil Search said the LNG project had commenced earlier than expected with relatively trouble free commissioning and ramp-up and an excellent operating performance both upstream and downstream.

The 120-day Lenders' Operational Completion Test for the LNG plant facilities was successfully completed in January 2015, with production significantly above the target rate and no project downtime.

"Joint venture parent guarantees will be released and loan repayments and co-venture distributions will commence once the outstanding lender requirements to achieve Project completion are satisfied," the company said.

By the end of December, 55 LNG cargoes had been lifted and 51 sold, while 23.5 equivalent cargoes of Kutubu Blend, comprising production from the PNG oil fields and condensate from the PNG LNG Project, have been sold with more than 90 cargoes expected to be loaded in 2015.

Oil Search said the average realised LNG price in the December quarter increased by 7% to US$14.33 per million Btu, comparable with spot prices fetched for early LNG shipments when Kutubu Blend was fetching US$111 a barrel. However, prices for Kutubu Blend fell 27% to US$73.64 a barrel in the December quarter.

It said the average price realised for LNG shipments in the December quarter reflected the commencement of long-term LNG contracts "and the approximately three month lag between the spot oil price and LNG contract prices".

MOU Signed on P'nyang and Domestic Gas Supply Deal

The PNG Government has signed a Memorandum of Understanding with ExxonMobil for possible expansion of the PNG LNG Project, pending award of a Petroleum Development Licence and further studies on the P'nyang gas field in PRL 3.

Under the agreement, ExxonMobil will undertake to provide up to 20 million cubic feet of domestic gas daily for power generation in Port Moresby and Hides as well as 25 megawatts of electrical power for Port Moresby in the near term.

ExxonMobil, operator of the PNG LNG Project, said the gas supply agreement was in addition to the existing gas commitment for domestic power generation at Hides.

The provision of 25MW, about 20% of generating capacity in Port Moresby, will be provided for an interim period while the government addresses long-term power generation options. "The remainder of the gas supply will be used to fuel a new state-owned gas fired power generation unit expected to be located near the LNG plant outside of Port Moresby.

The National newspaper, which attended the signing ceremony, quoted Prime Minister Peter O'Neill as saying ExxonMobil had agreed to supply 25MW in June and an additional 50MW in the next six months.

The agreement provides for the awarding of a PDL for the P'nyang field and associated pipeline licences to provide long-term gas supplies for power generation and to enable expansion of the PNG LNG Project, including the possible development of a third LNG train.

Preparations will be made to drill an appraisal well at P'nyang within two years of the awarding of the PDL.

A separate statement by Oil Search said appraisal drilling and development engineering studies will begin this year with expectations the PDL will be offered by the end of the first quarter.

The strategic review Oil Search completed in October last year said provision of adequate power supplies in PNG was becoming "an emerging political and social issue". It said electricity penetration in the country "is one of the lowest in the world" with an estimated 6% of the population having access to delivered power.

It noted that electricity prices in PNG were among the highest in the world and that poor and unreliable services were a constraint on industry development.

Oil Search was reviewing a number of power solutions, including small scale LNG for the Highlands and remote power supplies; gas generation from peripheral fields and a biomass project for a northern power grid.

Oil Search 2014 Results Reflect Lower Oil Price, and Buoyant LNG Contract Prices

Oil Search Ltd has announced that its average crude oil and condensate price had fallen by 27% to US$73.64 a barrel in the December quarter, from US$100.67 in the September quarter, while prices for LNG and gas sales rose by 7% to US$14.33 per million Btu.

As a result of higher production from the PNG LNG Project, Oil Search said total operating revenue in the fourth quarter had risen 4% to US$562.1 million to take total operating revenue for the year to US$1.61 billion or more than double the 2013 figure of US$766.3 million.

The company noted that the improvement in the LNG price reflected the start of long-term LNG contract sales "and the approximate three month lag between the spot oil price and LNG contract prices".

Since the end of the December quarter Brent crude oil prices, which closely match the Kutubu blend, have fallen to around US$50 a barrel.

While emphasising that Oil Search "is well placed to manage the current low oil price environment", the company said it was conducting a comprehensive review of impairment across all its assets given the rapid fall in oil prices. It currently anticipated a pre-tax impairment charge in the range of US$150-200 million for the 2014 year. This related primarily to reductions in the carrying value of some exploration licences in PNG and certain Middle East/North African assets.

Financial results for the year to 31 December 2014 will be released on Feb. 24 with expectations that the effective tax rate for 2014, prior to any impairment charges, will be in the range of 35-39%.

NPCP Arranges US$520 Million Financing and Concludes Deal Worth US$1.342 Billion

The National Petroleum Company of PNG (NPCP) has arranged financing of US$520 million through a banking syndicate made up of ANZ, BSP and Westpac.

In a statement, NPCP said it had undertaken a series of transactions totalling US$1.342 billion prior to the end of 2014.

This had enabled NPCP to take up the Government's interest in 149,390,244 Oil Search shares and to repay an existing Bridge facility to UBS and to fund working capital requirements for its existing licences.

NPCP Managing Director, Wapu Sonk said the purchase of Oil Search shares met with NPCP's strategic objective of increased participation in all oil and gas business in PNG.

NPCP Purchases Cue Energy’s PNG Assets for US$7 Million

The National Petroleum Company of PNG (NPCP) has purchased the PNG interests of Cue Energy Resources Ltd for US$7 million cash effective 20 November 2014, Cue Energy announced on December 24.

Cue said the sale of its wholly-owned subsidiary, Cue PNG Oil Company Pty Ltd, substantially exceeded the book value of its assets. It said the sale was in line with the company's strategy of operating in lower cost areas with near term development options. Cue also has operations in New Zealand and Indonesia.

Cue's Chief Executive David Biggs said the sale of PNG assets "allow Cue to realise value from its share of the declining reserves and contingent gas resources and releases Cue from a potential substantial well commitment of up to US$10 million, delivering a material saving over the short to medium-term."

The company's Chairman, Geoffrey King, signalled the sale of the PNG assets in his address to the company's annual general meeting on Nov 27 last year. Assets sold by Cue were - PDL3 (5.568892%); SE Gobe Unit (3.285646%); PRL9 (14.894%); PRL14 (10.94%).

INDUSTRY NEWS - MINING

Cost Margins at Lihir and Hidden Valley Fall into the Red

Newcrest Ltd's Lihir gold mine and its 50% owned Hidden Valley operation continue to be the group's worst performers with both mines reporting operating losses during the December quarter.

Newcrest said Lihir's December quarter production increased by 4% compared with the September quarter but performed below expectations largely as a result of unplanned maintenance issues.

It said the higher production was due to more ore being sourced from open pit operations, a higher percentage of ore being fed directly to the autoclaves and a marginal increase in head grade. This was partly offset by lower recoveries and unplanned maintenance in the conveying circuit, grinding circuit and autoclaves 1 and 4.

Australian dollar production costs had risen by 4% due to the weakening Aussie dollar exchange rate against the US, while it decreased by 1% in US dollar terms due to higher production and a favourable inventory charge movement.

All in sustaining cost at Lihir was US$1,240 per ounce (A$1,445), down from US$1,253 (A$1,353) in the September quarter, with a negative cost margin of US$37 (A$43) compared with a positive margin of US$37 (A$40) in the previous quarter.

At the Hidden Valley joint venture with Harmony Gold an employee fatality on December 6 and a mill shutdown till Christmas Day plus other maintenance issues and bad weather conditions contributed to a significant rise in overall production costs.

All in sustaining cost at Hidden Valley amounted to US$1,518 per ounce (A$1,769) compared with US$1,165 (A$1,257) in the previous September quarter. This led to a negative cost margin of US$315 (A$367) an ounce compared with a favourable cost margin of US$126 (A$136) in the September quarter.

Anglo-American to Sign JV Deal with Highlands Pacific

Highlands Pacific Ltd said it expects to conclude a deal on February 5 for a joint venture and farm-in agreement with a subsidiary of Anglo American plc for its Star Mountains copper-gold project.

It said Anglo American has completed its due diligence on the project, located near the Ok Tedi mine, and is at an advanced stage of planning a drilling campaign, with exploration to commence in the first quarter of this year.

The Star Mountains exploration tenement covers 515sq km and is located within the prospective New Guinea Orogenic Belt, which hosts the Grasberg, Ok Tedi, Porgera and Hidden Valley mines.

Exploration over the past three years has identified significant copper and gold mineralisation.

Meanwhile, Highlands is also forming a joint venture with Japan's Sojitz Group to develop its Sewa Bay nickel laterite project (EL 1761) on Normanby Island in PNG.

Highlands said that under a proposed farm-in agreement Sojitz would become the majority partner responsible for funding further drilling programs and studies. An initial six-month program will commence early this year costing around US$465,000 involving 1,500m of auger drilling and the assaying of 1,500 samples.

PNG Landowner Company Eyes Solomon Islands Project

The Lihir landowner company, Anitua Ltd has signed a strategic partnership agreement with the Australian-listed Axiom Mining to advance development of the Isabel Nickel Project in Solomon Islands.

Anitua has provided an unsecured loan of A$5 million to Axiom and they have agreed to negotiate arms' length commercial terms for provision of a range of services by Anitua for the Isabel project.

Axiom's Chief Executive Ryan Mount said: "There is a natural synergy between Axiom and Anitua - both companies are experienced in working with local communities in the Pacific, with a focus on collaboration and capacity building to ensure successful long-term operations."

Axiom has been awarded costs of A$4.7 million by the Solomon Islands High Court following a September 14 court decision against Japan's Sumitomo Corporation. Sumitomo has lodged an appeal and could be forced to pay nearly A$10 million if it loses the appeal.

Axiom has a 50-year registered lease and Prospecting Licence over the Isabel Nickel deposit and is hopeful of being able to commence a direct shipping ore operation within 12 to 18 months.

Anitua has become one of PNG's largest landowner companies since its establishment on Lihir Island in 1989. It employs over 3,500 people and has investments in Australia and PNG. It has a range of subsidiaries with capabilities in contract mining, road work and civil construction, mine site support and earth moving and mining training services.

Resource Sector Landowners get Model Trust Fund

Barrick (Niugini) Ltd has set up a Resource Base Trust Fund to provide an external investment vehicle that will enable landowners to invest their relocation packages and receive an annual income even after the Porgera mine closes.

The vehicle is open to landowners from other resource areas and representatives of Barrick or the fund manager, Pacwealth, have offered to make detailed presentations in Port Moresby or at relevant resource industry sites.

There is no similar vehicle available to landowners at the various mining and petroleum sites. The fund has already been well received by landowners in the Porgera area. The majority have agreed to receive a cash payment in lieu of having a relocation house built for them, but funds they receive must be invested in the Trust Fund.

Barrick has applied to the Government to confirm that all payments received by landowners will be non-taxable.

In a letter to other PNG-based mining companies, Barrick's Manager Commercial Services, Christopher Trainor, said: "Barrick believes there are many advantages to other mining and petroleum projects electing to utilise the Trust Fund for their landowners, including the ability to use an existing facility that is fully approved by the Investment Promotion Authority, a fund that is managed by a recognised PNG entity that is currently the investment advisor to Nasfund."

Trainor said it had taken four years to establish the Trust Fund. Landowners can elect to either receive a guaranteed annuity each year in quarterly instalments or quarterly instalments based on the returns on the invested funds.

INTERNATIONAL NEWS

Price Declines May Engulf All Major Commodities, says World Bank

The World Bank's Commodity Markets Outlook, released on January 22, said 2015 "may well see a rare occurrence for world commodity markets - a decline in all nine key commodity price indices".

It said oil prices have seen the most dramatic decline, the third largest fall since World War II, but other commodities have also been gradually weakening in recent months. "This broad-based weakness is expected to continue throughout 2015, before beginning a modest turnaround in 2016," the World Bank report said.

The report described the plunge in oil prices as being due to a "perfect storm" of conditions since the middle of last year. Among the factors were the growth in unconventional oil production, decline in demand, appreciation of the US dollar, receding geopolitical risks and a major redirection towards maintaining market share rather than targeting prices by the world's oil cartel, the Organisation of Petroleum Exporting Countries (OPEC).

Noting that oil prices had dropped 55% in seven months, it said that if the current slide continued it could surpass the previous record of a seven-month decline of 67% that occurred in 1985-86 and a 75% drop in 2008.

Near identical declines of more than 35% each have been experienced between early 2011 and the end of 2014 by the World Bank's three industrial commodity price indices - energy, metals and minerals, and agricultural raw materials. These prices were expected to further decline this year.

In addition, prices of precious metals were also expected to decline by 3% this year on top of the 12% drop last year due to ample supplies, weak demand and a strengthening US dollar.

The World Bank is presently forecasting that oil prices this year will average US$53 a barrel, 45% lower than in 2014. The fall in oil prices will also impact other commodity prices, especially natural gas, fertilisers and food commodities.

Metal prices were forecast to drop by more than 5% this year with the price recovery that is likely next year anticipated to be "small compared to the depths already reached".

TO ALL CHAMBER MEMBERS:

THE 2015 MEMBERSHIP INVOICES HAVE BEEN SENT OUT IN JANUARY AND ALL MEMBERS ARE REQUESTED TO RENEW YOUR MEMBERSHIP UPON RECEIPT OF THE INVOICE AND THE STATEMENT OF ACCOUNT. PLEASE DISREGARD THIS MESSAGE IF YOU HAVE PAID YOUR 2015 FEES INCLUDING ANY OUTSTANDING INVOICES AND HAVE SENT US A REMITTANCE ADVICE.

IF YOU ARE A CURRENT MEMBER AND HAVE NOT RECEIVED AN INVOICE OR A STATEMENT OF ACCOUNT FROM THE CHAMBER YOU ARE KINDLY ASKED TO CONTACT THE FINANCE TEAM AT THE CHAMBER SO WE CAN UPDATE YOUR CONTACT DETAILS AND FORWARD THE INVOICES TO YOU DIRECTLY.

THE CHAMBER WISHES TO THANK ALL MEMBERS FOR YOUR ONGOING SUPPORT AND COMMITMENT IN HELPING US TO SERVE YOU BETTER.