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Incitec lures Cottee back to Qld seam

So it is back to the future for a fourth time for Richard Cottee.

Cottee is the gas whisperer who turned Queensland Gas from near-broken penny dreadful into the $5.7 billion takeover target that seeded what is Royal Dutch Shell's LNG business in the Sunshine state. Now, a dozen years and two companies later, Cottee has been invited back to coal seams of Queensland. And, once again, he has arrived with a very familiar, ever-entrepreneurial customer in tow.

The tie that binds each and all of Cottee's past successes to his Macarthur-like return to southern Queensland coal seams is Incitec Pivot. The gas-hungry chemicals maker has made a habit of putting present and future supply contracts where Cottee's mouth is.

Cottee has always maintained that QGC shareholders would never have got the pay-day they did had Incitec Pivot not delivered him an early-stage, company-making supply deal.

And, even further back in Australia's gas age, when Cottee was a Santos man, it was Incitec's determination to lure new supply into the Queensland market that helped deliver South Australia's gas company a new horizon in the south-west of the state.

Since the 2006 sale of QCG to BG Group (which was, in its turn, eaten by Shell) Cottee has taken a crack at unlocking value in offshore West Australian gas and at bringing new life to the Northern Territory's southern gas.

The WA gamble with Nexus Energy ended in internecine conflict and frustration, while the effort to promote the latest vehicle of his restless ambition, Central Petroleum, as part of the answer to the east coast gas shortage, is a game still very much in play.

Once again, Incitec was an early backer of Cottee's vision, providing direct funding through an issue of convertible notes and future custom should Central get its gas into the new pipeline that will link NT gas with east coast markets through Mt Isa.

And now, through a twist of familiar fate, Incitec has proven pivotal in

Richard Cottee has the backing of gas-hungry Incitec Pivot. PHOTO: JIM RICE

manufacturing Cottee's return to where it all started, to the coal seams of Queensland.

On Thursday, Central won the tender for new gas tenement released by the state government. Cottee arrived at that successful pitch with an investment partner and a customer all in one. Yep, you guessed it, Incitec Pivot.

Once again, Incitec is offering itself as a future customer if Cottee's people can lure gas from coal seams that have historically proved productive. But there is more. Incitec will pay up to $20 million of the drilling and appraisal costs that it hopes will result in production by 2022.

Incitec chief executives past and present deserve great credit for so consistently working to invite gas supply solutions. This time around the aim appears to be to sustain its Gibson Island fertiliser plant, which chews through about 15 petajoules of gas every year. That represents maybe 12 per cent of the state's industrial gas demand.

The Brisbane plant's gas contract was written a decade ago so presumably the pricing reflects that gas was plentiful and was extracted at a lower cost. But the contract expires this year and times have changed. Incitec says it cannot get contract tenor or pricing terms that allow it to keep Gibson Island running.

As a result, Incitec now has overlapping supply arrangements with Cottee and Central that work to, at very worst, buy time for Gibson Island. Incitec said on Thursday that it is negotiating access to Central's NT gas production "at least until the end of 2019". At that point the three exploration wells required to be drilled on Central's new Queensland tenement (PLR201718-1-1) over the next two years will have revealed whether or not there is anything commercial there.

That tenement is only just west of Brisbane (in gas industry terms, at least), so delivering gas to Gibson Island would be comparatively and definitively cheap.

Given the potential is made real, then Incitec would need to find another two or three years of gas to feed Gibson Island while it waits for first gas from Central's new play. But that might fit nicely with the wider Central development schedule, a program that is being held up, in part, by the competition regulator's concerns over marketing plans.

"The irony for us is that it is the ACCC that is currently the biggest barrier to our entry into the east coast market," Cottee told *The Australian Financial Review* on Thursday.

The starting point of Central's growth story is revitalisation of the Mereenie gas field. Its 50 per cent partner in that project is Macquarie Bank. And they want to use their gas to fill the currently unallocated capacity of the pipeline to the east that Jemena will have built by year's end.

The pipeline will arrive with a capacity of 90 PJ. So far 32 PJ of that space is allocated to gas that the NT government ambitiously acquired from the ENI operated Blacktip gas project in the Timor Sea.

The Central-Macquarie plan would see Mereenie production run at 63 PJ annually with 15 PJ of that headed into the NT market and the balance headed east through Jemena's pipe. Beyond that Cottee has plans to add another 20 PJ to his offering from gas produced at his Palm Valley field.

But Macquarie wants to market the gas jointly with Central and to do that the partners need ACCC approval.

Now, the rather odd thing about this is that the ACCC did not appear to have any problems with Macquarie's move last year to own all of Central. That deal, which was ultimately stymied by Cottee's shareholders, would obviously have resulted in something even more aligned that "joint marketing" of Central's gas.

But, having finally unlocked the joint marketing of gas by the Bass Strait ventures, Exxon and BHP, the ACCC seems determinedly reluctant (understandably perhaps) to indulge joint marketing of gas volumes in what is an illiquid market.

While we are talking east coast gas markets, we hear that the bloke with LNG re-gas on his mind, James Baulderstone, says he is loving his new place on the virtuous side of the great Australian energy debate.

In a pretty recent past executive life Baulderstone had the task of running Santos' east coast gas business. That left him on the front line of the deeply fractured NSW coal seam gas debate and of managing the fallout from the dawning of awareness in political capitals that turning on three giant LNG export projects pretty much at the same time might turn domestic markets upside-down. One of the pillars of Baulderstone's pitch is that the outlook for future Australian gas production is nothing like as secure as the official forecasters have presented.

The most recent AEMO outlook, which is worrying enough, quite frankly, describes lower volumes of gas headed into domestic markets over the next two years. Beyond that the output from producing fields falls off a cliff and the gap is filled increasingly by production from proved and probable resources (2P). From 2025, that 2P production falls on a cliff and it is filled by the introduction of gas from fields containing gas currently classified as contingent resources. Then that falls off a cliff from 2030 and future domestic demand is covered by gas that is yet to be even discovered.

Baulderstone's problem is that a whole lot of that 2P and contingent resource is booked from onshore gas that is trapped in coal seams or shales. He worries that future coal seams will not be as productive as the first generation that feeds all three of Gladstone's LNG plants and that future shale developments will be more challenging and far more expensive than the optimists might imagine.

In this view he has a supporter in Richard Cottee.

"There is many a dry gully before you hit the water course," the coal seam gas pioneer observed. "Markets will always get into balance, but the way things are, the only way that is going to happen is demand destruction. It is just dangerously wrong to assume that 2P or 2C resources were created by German and Japanese engineers and that their quality control is superbly consistent. The next generation of coal seams will be more like a 1960 British car. Sometimes they will be gorgeous. But there will be others that will need to spend a lot of time in the garage.

"The thing is that, back at the start, no one ever imagined that Queensland would own 70 per cent of the east coast gas market. Queensland was going to be the add-on that made export markets happen rather than the national engine room."