

TIMOR LESTE AS AN LNG EXPORTER

WHY NOT?

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The Benefits of Becoming an LNG Exporter

- US\$ 1.5 billion foreign direct investment, perhaps 50% spent in Timor Leste
- US\$ 60 million annual operating expenditures, perhaps 50% spent in Timor Leste
- Thousands of direct and indirect jobs
- Hundreds of technical and management training opportunities
- Creation of locally-owned service businesses
- Gas for domestic use, replacing imported oil
- National pride and self respect

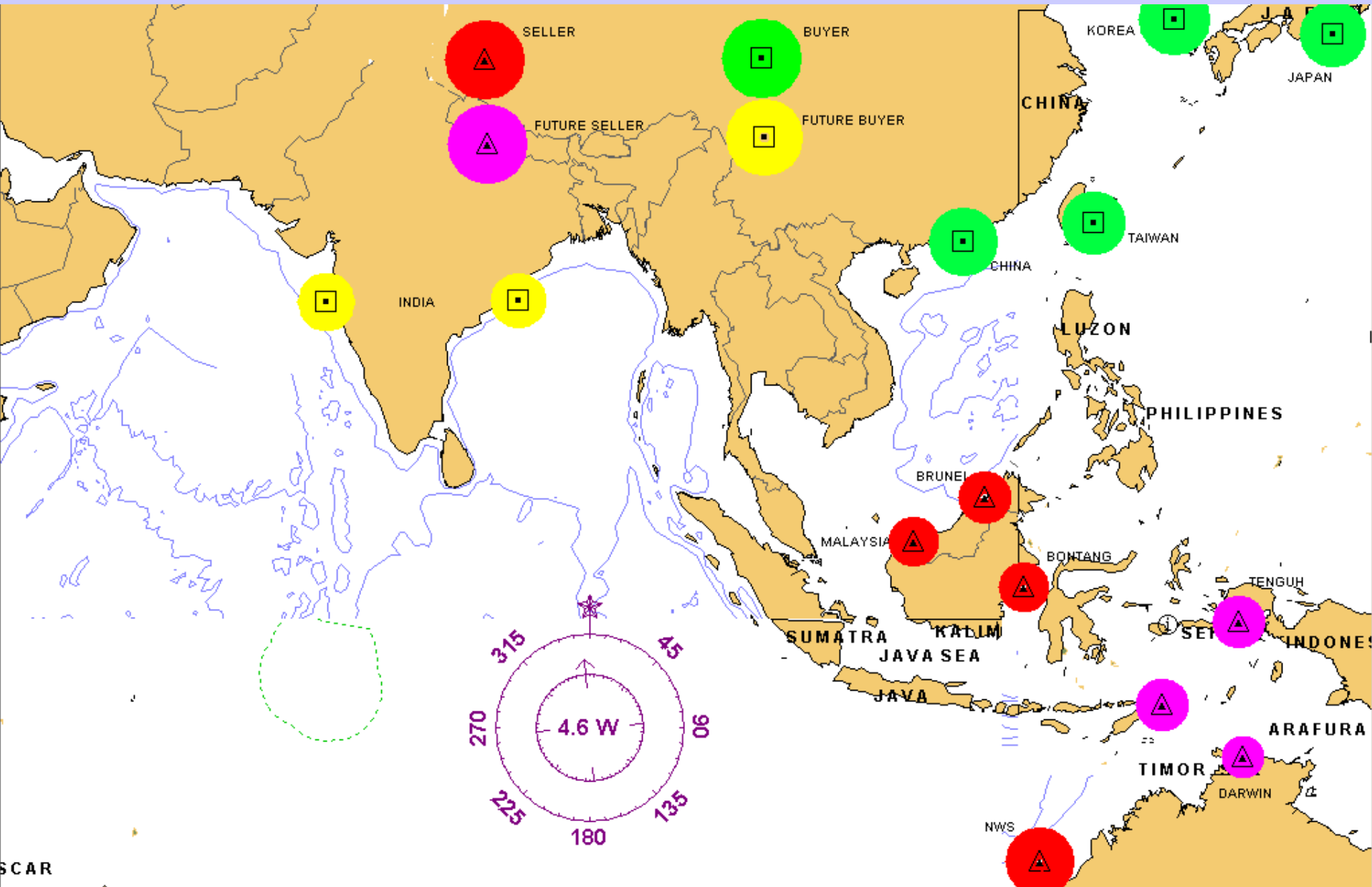
A Worthwhile Goal, *but*

- Timor Leste will have to compete with Australia to attain this goal
- You have several advantages over the competition *but one serious disadvantage*:
 - New nation
 - No financial performance history
- This can be mitigated with diligent efforts

Global LNG Trade

- Capital intensive
- Long-term contracts – 20 years, often 20 more
- Extremely competitive
- Dominated by big players
 - Major energy companies
 - Major exporting countries
- However, Bontang in 1970s was an exception
 - Pertamina + small U.S. company Huffco
 - Built an industry where there was nothing
 - Gas producers don't own LNG plant; Pertamina does

LNG Sellers & Buyers



Timor Sea Gas Today

Bayu Undan

- Oil production/ gas recycling under construction
- Oil production start-up in early 2004, with revenues for Timor Leste
- Gas reserves estimated at 3 TCF
- Proposed LNG plant in Darwin, one train with output of 3+ mtpa; Japanese buyer
- Darwin LNG plant “on hold” pending treaty ratification by Australia
- Single-train LNG projects are very difficult economically

Timor Sea Gas Today

Greater Sunrise

- No firm production plans yet
- Gas reserves estimated at 7 to 9 TCF, which could support LNG plant of 1 to 3 trains, up to maximum of 10 mtpa output
- No announced buyer or commitment for LNG plant at this time
- Operator intentions unknown
 - Operator rejects Darwin option
 - Floating LNG facility?

LNG Plant in Timor Leste

Assumptions

- “TimorLNGCo” plant with 2 trains and output of 6.6 mtpa output needs 6+ TCF gas reserves
- Sunrise reserves of 7 to 9 TCF adequate
- Gas would be purchased at Sunrise platform by “TimorLNGCo”
- “TimorLNGCo” output *must* be price competitive in the region

“Timor LNGCo”

Critical Economic Variables

INPUT:

- Cost to purchase gas from Sunrise
- Pipeline costs from Sunrise to Timor Leste
- LNG plant construction costs on Timor Leste
- Tax structure for LNG plant
- Cost of capital (country risk)

RESULTS:

- LNG export price *must* be competitive in region

COMPETITIVE ADVANTAGES

Timor Leste vs. Darwin

	TIMOR LESTE	DARWIN
Gas Cost	no difference	no difference
Pipeline Cost	advantage	
LNG Plant Cost	advantage	
Tax Structure	advantage	
Cost of Capital	disadvantage	advantage
LNG EXPORT PRICE	ADVANTAGE!	

Gas Cost = No Difference

- The price for gas at Sunrise depends on field development economics
- Assume the same gas price regardless of destination, Darwin or Timor Leste
- Assume the gas will be produced under existing tax and royalty arrangements
- Therefore, Timor Leste revenue remains the same

Pipeline Costs = Advantage

- A pipeline for 2 LNG trains can be laid to Timor Leste for less than to Darwin
 - Deeper water, but very feasible
 - Smaller pipe, shorter distance
 - Can be done with existing equipment
- Cost is 1/2 to 2/3 of a pipeline to Darwin
- Two pipeline engineering studies and two pipeline constructors confirm

LNG Plant Costs = Advantage

- An LNG plant in Timor Leste could be built for 5 to 10% less than the same plant in Darwin
 - Modular construction, assembled on site
 - Non-union skilled overseas labor
- Two global construction firms confirm

Tax Structure = Advantage

- Point to remember: If no LNG plant in Timor Leste, no plant taxes ever
- Therefore Timor Leste can offer “zero- cost” tax incentives that improve project economics, to attract foreign direct investment and job creation
- Offer “tax holiday” for first 10 years of LNG plant’s 20- to 40-year life
- Exempt LNG plant from import duties, VAT, other levies

Cost of Capital = Disadvantage

The Main Issue for Timor Leste

- New nations are perceived to have higher country risk
- Investors fear:
 - Unrest, violence, national strikes
 - Changes in tax rules and business law
 - Other anti-business sovereign acts (nationalization, confiscation)
- Cost of capital for Timor Leste cannot be established without MLA affiliation and participation
- In future, cost of capital for Timor Leste projects may be 2 to 6% above Australia's cost of capital
- Foreign company equity investors will also expect higher returns for a Timor Leste plant

Mitigating Country Risk: What Investors Want

- Rule of Law - absence of corruption
- Transparency of agreements
- Improving conditions for the population
- Investment in project infrastructure by World Bank, ADB, other MLAs
 - Example: World Bank financed Thai offshore pipeline, loan repaid with pipeline tariff income

Mechanisms for Reducing Country Risk

- Write agreements subject to law of a long-established nation (U.K., U.S., e.g.)
- Offshore trust accounts distribute revenue to investor participants
- Host country forms close, productive affiliation with multilateral lenders (MLAs)
- International institutions (MIGA, OPIC, e.g.) insure some of the political risk

“TimorLNGCo” Export Price

INPUT:

- Same cost of gas for either destination
- Lower pipeline and plant costs for Timor Leste
- 10-year tax holiday, zero VAT and import duties
- 2% premium for equity investor returns
- 4% country risk premium for loans

RESULTS:

- LNG export price from Timor Leste could be 10 to 20% lower than from a Darwin LNG plant

Suggested Next Steps

- Act now before alternative decisions are made
- Encourage the Sunrise operator to evaluate Timor Leste as an LNG site
- Actively affiliate with MLAs, discuss project
- Seek project developers willing to undertake their own studies of a Timor Leste LNG plant
- Become experts in LNG business and finance; there is plenty of help available
- This expertise will serve you well whatever the outcome
- *A major opportunity deserves a major effort*