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Looking over the horizon

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Fresh from a \$US40 million-plus investment to almost double Horizon Oil's stake in an oil project in China, chief executive Brent Emmett is looking forward to further growth in the explorer's core regions in China, Papua New Guinea and New Zealand.

Horizon's decision to bulk up in China rather than conserve its funds for growth in PNG surprised some analysts, including Merrill Lynch, but Emmett is more than happy about the move, while still underlining the "material opportunity" provided by gas in PNG.



Brent Emmett, chief executive of Horizon Oil: keen to bulk up on reserves.

"We're big believers in the oil price," Emmett told Resources Daily. "Now is a good time to get hands on as many reserves as we can."

Horizon took the view that the first place to look to add reserves was around its current assets and had been eyeing fellow junior Petsec Energy's stake in the Beibu Gulf oil project for some time, knowing Petsec was a willing seller. Petsec is understood to have sought to sell the stake twice before, but each time the deal fell through because approval from venture operator CNOOC wasn't forthcoming.

According to Emmett, it was Horizon's good relations with CNOOC, its links with Petsec and its ability to follow through on the acquisition helped secure the asset earlier this month, at a price described by some analysts as a discount of about 40 per cent to its valuation.

The acquisition increases Horizon's share of reserves in the venture to 11.3 million barrels of oil, from 6.2 million, taking its stake in the project to almost 27 per cent. Australia's Roc Oil has a stake of almost 20 per cent in the venture, while CNOOC owns 51 per cent and Majuko Corporation about 2.5 per cent.

After finally reaching a long-awaited final investment decision on the Beibu Gulf project in February, first production is due to start up in late 2012. The first phase involves a 24 million barrel resource, with a second phase targeting a further 18 million barrels of oil.

Horizon issued \$US80 million of convertible bonds to finance the deal, help cover its share of development costs and to set the scene for financing the rest of its growth projects. With its increased stake, Horizon's share of the \$US300 million phase one project has risen to about \$US81 million.

The subordinated facility will not interfere with a planned senior debt issue of between \$US100 million and \$US150 million planned later this year once Horizon has sized up its funding requirements in PNG, Emmett said. The bonds can be converted into shares at the current equivalent of 49¢, about a 30 per cent premium to where Horizon shares were prior to the issue and about 45 per cent higher than the price of shares in a rights issue had the company gone down that path, he added.

Emmett, a geophysics graduate, started off in the industry as an explorationist, working for Exxon and Elf Aquitaine in Australia, Papua New Guinea and New Zealand. Taking up a position as exploration manager at Ampoex led to international business development roles, then a switch into investment banking as part of the oil and gas advisory team at CIBC World Markets.

He joined the board of Bligh Oil and Minerals - the previous incarnation of Horizon - in 2000 and the following

year founded an investor group, Oasis Energy Investments, which took a major stake in the company. That led to his appointment as chief executive in early 2002, from which time he has actively driven the build-up of Horizon's international exploration and development activities.

Horizon has already sought expressions of interest from four or five banks for the senior debt financing to cover its first gas condensates project in PNG and a potential expansion in New Zealand. A final investment decision on the \$US200 million Stanley project in PNG, owned 50/50 by Horizon and Canadian partner Talisman Energy, is expected in the second half, with first production in mid-2013.

The partners are yet to finalise marketing arrangements for the condensates from Stanley, but Emmett pointed to the InterOil refinery in Port Moresby or the two refineries in Brisbane, owned by BP and Caltex, as potential buyers.

Meanwhile, appraisal drilling at the Elevala and Ketu wet gas fields is due to get underway in the September quarter after the resolution of a dispute with the government over tenure of the resources.

The PNG petroleum minister decided in November not to renew Horizon's PRL 5 retention lease over the two fields, saying the partners had not fulfilled the conditions of the licence.

Emmett acknowledges there was some justification for the argument, given little work had been carried out in the permit for the last decade, but, convinced the minister had overstepped his powers, Horizon started legal proceedings.

The issue was eventually resolved by the government issuing a new licence, PRL 21, which would be 70 per cent held by Horizon and partner Talisman, with the rest being taken up by local companies Dabajodi and Elevala Energy. Horizon has since bought out Elevala's 10 per cent interest, taking its own stake to 45 per cent, while Talisman has 35 per cent and Dabajodi International Energy 20 per cent.

Emmett is satisfied with the compromise, noting that the alternative would have been to pursue the judicial review, inevitably delaying drilling at the fields when a rig was already ordered under contract.

Still, he says investors should not necessarily be concerned about political risk in PNG.

"What it says is that if you want to retain assets in PNG you have to get on and develop them," he says.

Condensates output from Ketu and Elevala is expected to follow the start or production at Stanley, with production of natural gas from the fields further down the track.

It is the gas that provides the "material opportunity", Emmett says, with potential production through a stand-alone onshore or floating liquefied natural gas project, or from supplying gas to a third or fourth train at ExxonMobil's LNG venture currently under construction.

Whatever the eventual commercialisation route, Horizon will not look to participate in the capital-intensive liquefaction part of the project but will look to sell gas to the LNG project.

"PNG is really the big upside for Horizon Oil," Emmett says.

Meanwhile in New Zealand, Horizon is considering the potential for a second phase of development at the Maari oil field in the Taranaki Basin, operated by Austria's OMV. A final investment decision there is likely later in 2011 or early in 2012.

"It's fairly clear that is something we want to participate in."

The expansion plans should drive a substantial growth in production volumes at Horizon from today's output of about 1500 barrels a day from Maari. A production forecast presented by chief financial officer Michael Sheridan at the UBS conference last week shows output surging from an estimated 2000 barrels a day in 2012 to over 10,000 barrels a day in 2014 on the back of the Beibu Gulf and PNG condensates ventures, then to peak at over 17,000 barrels a day in 2017 when the PNG gas flows start up.

Merrill Lynch analysts James Bullen and David Heard agree the growth profile of the company, which they rate as a buy, looks attractive, noting that the increased China stake lowers the risk of the expansion ambitions, which do not substantially rely on further exploration success.

The analysts have a 47¢ price target on Horizon's shares, which have been flat over the past 12 months, broadly in line with the S&P/ASX 300 Energy index. The price objective is more than 50 per cent higher than Tuesday's close of 31¢.

Horizon now has 12 million barrels of proven and probable oil reserves associated with already sanctioned or producing projects, and the potential for a further 20 million barrels to be sanctioned in 2011 and 2012, Merrill Lynch said, noting also the quality of the junior's venture partners, in CNOOC, Talisman and OMV.

The Australian Financial Review

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