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AJ's UK shale drawcard faces its test

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It has taken longer and cost more than expected, but AJ Lucas and its UK affiliate Cuadrilla Resources are now just months from getting results that could demonstrate the commercial viability of massive shale gas resources in north-west England that could transform the country's energy position.

With Cuadrilla's licences thought to hold several hundred trillion cubic feet of the 1329 tcf of gas estimated to be in the Bowland shale, the results from the fracking of the UK's first two horizontal wells are set to be closely watched across the UK and beyond.

Certainly 2018 has shaped up to be "very important" for the companies involved and the UK's nascent shale industry, said Cuadrilla chief executive Francis Egan, who is undaunted by the noisy protests over the company's operations and the time taken to get to this point. "The rock quality is perfect for fracturing; really we just need to get on with it," said Mr Egan, a former head of global petroleum production at BHP, before kicking off a roadshow of AJ Lucas investors in Sydney, Melbourne and Hong Kong.

"You can't talk the gas out of the ground," he said, noting the intention of having the first Lancashire shale gas flowing into local houses in 2019.

Cuadrilla, which is about 45 per cent owned by each of AJ Lucas and US private equity firm Riverstone Holdings, is partnered in its Preston New Road shale project near Blackpool by Britain's largest household gas supplier Centrica, keen to secure a new local source. For AJ Lucas, which also has a 23.75 per cent direct interest in the Bowland licences, the UK shale asset is the biggest on its balance sheet and the main draw for investors in recent years, said chairman Phil Arnall. "We didn't foresee the challenges in front of us both in time and cost," Mr Arnall said. "But you've got to look at the positives: we're now at an exciting stage. In the next six to nine months we will start to see the outcome of all of those years of hard work by these guys."

Along for the ride is AJ Lucas' second-biggest shareholder and Rich Lister Paul Fudge, who made a fortune from early investment in coal seam gas in Queensland and who is a major player in Northern Territory shale exploration through Pangaea Resources. Its majority shareholder, private investor Kerogen Capital, is also a backer of another UK shale explorer, iGas Energy.

The prize is large: even if only 10 per cent of the British Geological Survey's estimate for Bowland shale gas is produced, it would meet the UK's demand for gas for about 50 years. Declining North Sea output means the UK's reliance on imports is set to increase from about 50 per cent to 80 per cent by 2030.

While supported by a government in the middle of the UK's worst squeeze on gas for a decade, the Preston New Road project has attracted fierce protests from environmental groups worried about water and land contamination, seismic tremors, local traffic and the broader impact on climate change.

Repeated appeals have delayed the project, while consent for drilling at Cuadrilla's second Bowland venture, at Roseacre Wood, is still pending subject to public inquiry into road safety issues. Fracking has been banned altogether in Scotland.

The delays mean that a £60 million (\$110.4 million) investment by Centrica that was intended to fund the drilling and fracking of the first two wells at Preston New Road was used up by February, with drilling of the second well and any fracking still to come.

AJ Lucas, which has a market value of about \$247 million, has streamlined its Australian drilling and mining services operations in recent years to focus resources on the UK shale activity.

Cuadrilla is aiming to start fracking in July, by which time the second horizontal well would be drilled, with "meaningful" results seen in the September quarter, Mr Egan said.

The first well, the first horizontal shale gas well to be drilled in the UK, was completed earlier this month. Drilled to a depth of about 2700 metres, the well then extends laterally about 800 metres through a shale gas reservoir that is about a kilometre thick.

Patersons has tentatively valued AJ Lucas's interest in the Bowland at \$3.4 billion-\$6.4 billion, assuming about 30 tcf of gas is ultimately recovered.

Cuadrilla has estimated the first two horizontal wells will cost about \$US30 million each to drill frack and complete, Patersons noted. The broker says that, assuming costs can be reduced to about \$US15 million (\$19.8 million), about 8 bcf of gas would need to be produced from each well to be commercially successful.

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