

## SMALL COMPANIES IN THE PETROLEUM MARKET

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### ABSTRACT

The challenges facing the promoters of start up companies in the hydrocarbon sector are immense. Convincing investors that your particular project is better than the hundred other projects that they have seen is one thing, convincing them that they would be better off buying your paper than the plethora of equities that they could acquire with their discretionary dollars is another. As a result of these considerable challenges a start up company has to occupy a space that no one else is in. For instance I'm sure that promoters floating companies on the back of recently acquired Cooper Basin exploration assets have heard the response a thousand times: 'why would I buy your stock when there is any number of listed Cooper Basin stocks, big and small that I can invest in'.

So the challenge is to find a niche that no one else is in and occupy it. A downside of this is, of course, that no one really understands what you are doing, so there is an instant credibility gap that must be overcome.

When AusAm Resources was formed in late 1999 with the objective of exploiting tight gas resources in Australia, we pretty much had this space to ourselves. Initially the Australian equity market was sceptical, however in recent times we have seen several competitors both locally and from overseas compete for this space in our sector. These players have recognised the importance of treating some of the poorer quality reservoirs with care. This broader acceptance of this has been a result of some decent drilling results in the Surat where under balance drilling has become more commonplace.

The idea in forming AusAm Resources was to exploit existing tight gas resources in Australia by using routine technology developed in North America but which was relatively under utilised in the Australian market. This technology had been developed in the US and Canada largely in response to a tax incentive that the US had established, such that their very large resource base in tight rocks could be exploited rather than being absolutely dependent on imported hydrocarbons. This process has been successful and now there are several service companies that are dedicated to providing the necessary staff and equipment to achieve under balanced drilling and completions. The technology is not unique, but its application requires careful planning to ensure that it is conducted safely and successfully. We would contend that this requires a dedicated engineering planning phase, based on experience in this area. This is because it is not just an extension of conventional drilling; it is a distinct vocational area and demands the attendant experience and attention to detail.

AusAm started out by buying a big slice of the Perth Basin, which contained two known gas fields, Walyering and Warro. The prospectus was written and put into a very tough resources sector in June 2000. The raising was aimed at A\$5 million and we managed about half of that, and of course had to send it back, as it failed to raise the required minimum. The second step was to encourage a group of Texans who we had met and were enthusiastic about what we were doing. This private capital has continued to support the company whilst it developed a broader portfolio.

This development has been necessary because of the shape of the WA gas market. Some large companies dominate this market and as a result the competition for gas markets is intense and therefore it is difficult envisage an entrance for small amounts of gas into the market. In contrast the east coast gas market is more diverse and is not dominated as much by the larger companies, and of course the market is much larger. Thus in the past two years AusAm has evaluated several projects and has recently entered into a joint venture with Oil Company of Australia to appraise and develop the remaining potential of the Namarah/Warroon and Parknook fields. As well AusAm will be earning equity in the adjacent Werribone area, now known as the Formosa Downs joint venture.

The appraisal programme in these areas will consist of drilling several wells all using under-balance drilling techniques. The wells will target three reservoirs, the Showgrounds, Rewan and fractured basement. In the Formosa Downs area the Tinowon Sandstone is expected to be a target as a flank play on the well-developed plunging nose that makes up the major structural feature in this area. This reservoir unit is absent from the Namarah/Parnook fields has the potential to form a structural/stratigraphic trap within this unit.

AusAm, has recently been granted ATP 754, which is a large 1.5 million acre area on the southern and western margin of the Taroom Trough. OCA has joined AusAm, as an equal joint venture partner in this area. The exploration programme will be dominated by the pursuit of Tinowon Sandstone traps. Evidence from existing wells such as Cockatoo-1 would suggest that the Tinowon Sandstone will be an exciting exploration target in this area. Where this interval has been penetrated in the past explorers have observed excellent oil and gas shows and whilst some testing of these intervals has taken place there appears to have been a perception that the interval was tight. Whilst this is understandable, there is now sufficient evidence to suggest that the sandstone has a significant volcanic derived influence, often being described as a tuffaceous sandstone.

As a result of this rock type, it provides an excellent opportunity for conventional mud systems to invade this rock and hydrate the clays such that, what permeability was available is subsequently reduced. What is

encouraging about the Tinowon Sandstone objective is that it has the Taroom Trough adjacent to it to provide more than adequate hydrocarbon charge. Explorers in the Surat have recognised for many years that this basin has been overcharged, in that all the traps would appear to full, such that it has always been a matter of finding the trap. Thus the Tinowon Sandstone would appear to be emerging as a strategic new play development. Whilst it has been recognised as such in the past, it would appear that this potential will be aided by recognising that its volcanic influence, and the attendant clays, make it an ideal candidate to be exploited with under balance drilling.

AusAm will continue to pursue capital from the private equity market. This is deliberate tactic based on the observation that the Australian listed market treats its resource companies harshly. Recent floats are an example of this, where companies with good acreage and good management, trade below their issue price. Thus the incentive for new capital is always going to be limited, when investors see their equities trade below the issue price on the first weeks of a listing. Our view is therefore to avoid this market in the early stage of a company's development. Rather the aim is to develop the business to a point where it can be valued properly based on its hard assets and its cash flow. At this point the company would be liquidated through a trade sale and the funds return to the investors, all going well at a significant multiple.

## THE AUTHOR



Terence Maxwell Barr graduated with an Associateship in Applied Geology from Western Australian Institute of Technology (3 year tertiary course) in January 1975. Since that time he has pursued a career in the petroleum industry. Mr Barr has held senior management positions with the South Australian Oil and Gas Corporation (Chief Geologist), Santos Ltd (Exploration Manager, Cooper Basin) and Carnarvon Petroleum NL (Managing Director). Mr Barr established a petroleum consultancy practice in late 1999 and has attracted a client base in the industry in Western Australia. He is a Fellow of the Australasian Institute of Mining and Metallurgy and a member of the Petroleum Exploration Society of Australia. He co-founded AusAm Resources Limited (formerly AusAm Resources NL) in December 1999 and holds the position of Managing Director.

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