Santos latest to write down gas investments, as total Australia losses near $20 billion

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Santos has become the latest Australian gas company to write off the value of its gas investments, announcing that it expects to record a $1 to $1.1 billion impairment as a result of a crash in global oil and gas prices.

Santos revealed the impairment in a statement to the ASX on Tuesday, telling investors that due to a collapse in global oil prices, caused by Covid-19 triggered falls in energy consumption and which has flow-on effects on gas prices, it was forced to write down the value of its investments in the Gladstone LNG project.

Many companies, including Santos, had made investments in new oil and gas projects under the assumption that global oil prices would remain above $60 per barrel.

However, since the start of 2020, the combined effects of a Russian-OPEC price war and Covid-19 related disruptions, has sent the Brent crude oil price plummeting, at one point reaching negative prices. Oil prices have since stabilised at around $40 per barrel, forcing companies to revise down the value of the investments due to lower expected revenues.

The collapse in the oil price has direct consequences for the Asian gas market, with many contracts for gas based on prices that are pegged to global oil prices.

Santos joins a growing list of gas companies that have been forced to write off the value of gas investments in the wake of the Covid-19 outbreak.

Origin Energy indicated it would write-off $1.2 billion in value relating to two of its LNG investments earlier in July. This followed Woodside recording its own $6.3 billion hit .

The list of fossil fuel companies hit by Covid-19 related impacts has continued to grow. Oil Search announced its own impairment of up to $570 million. Ampol Limited (previously Caltex Australia), declined to issue a profit guidance to shareholders in June, citing both the Covid-19 pandemic and market volatility as creating too much uncertainty.

Global energy giant Shell recorded a massive $22 billion write-down on its oil and gas investments, including $8- $9 billion related directly to its Australian based projects.

Smaller players have also been impacted, with Strike Energy recording a $91 million impairment on its Cooper Basin gas project.

Chevron, the largest investor in Australia's oil and gas market, has yet to indicate what level of impact recent developments have had on its own business.

As a conservative estimate, the amount of reported Australian investment losses in the oil and gas sector has amounted more than $18 billion during the first half of 2020. This estimate excludes losses recorded by privately held companies that do not have the same public disclosure obligations of publicly listed companies.

Investor advocacy group the Australasian Centre for Corporate Responsibility said that the write-downs are some of the clearest indications that fossil fuel assets are starting to become stranded.

“Today’s writedown by Santos – on the back of Royal Dutch Shell, Woodside and Origin writedowns – is a clear demonstration that oil and gas assets are being stranded right now,” ACCR director for climate and environment Dan Gocher said.

“Santos is prepared to sacrifice the climate and local communities on the slim chance that the Narrabri gas field may be profitable in the hope that business conditions improve. These gas assets will eventually be stranded. Santos must see the writing on the wall and abandon the Narrabri project before burning any more shareholder capital.”

It is a powerful indication of the amount of financial resources that have been lost by the oil and gas industry during the Covid-19 triggered economic crisis, and how much of a drag the sector has been on the Australian economy, rather than a contributor to recovery.

There has been a chorus of calls from the clean energy sector for stimulus measures to be directed towards investment in new renewable energy, energy efficiency and storage projects, but the Morrison government has ignored these calls.

The Climate Council released its own “Clean Jobs Plan” on Tuesday, outlining a series of 12 potential measures where investments in clean energy projects could create as many as 76,000 new jobs over the next three years.

“Australia has seen steep job losses throughout the COVID-19 pandemic. But with the right policy measures, thousands of jobs could be created in large-scale renewable energy, ecosystem restoration and the collection and processing of organic waste,” AlphaBeta Director, Andrew Charlton, who worked with the Climate Council to produce the Clean Jobs Plan said.

“Most of the 12 stimulus options can leverage significant private investment for the Australian economy. Investment in pilot-scale green hydrogen facilities would unlock $4 for every dollar of public money; utility-scale renewable energy unlocks $3 for every dollar invested,” non-executive director and Climate Council board member, Sam Mostyn added.

The Climate Council estimates that its plan would require around 0.5 per cent of Australian GDP in public investment, the equivalent of around $7.2 billion or around a third of what has already been lost by the gas industry.

Santos takes $1.1b pandemic oil crisis hit

Australian Financial Review, Jul 21, 2020 – by Angela Macdonald-Smith

Write-downs by Santos of up to $US800 million ($1.13 billion) have axed $US7 billion of asset value from ASX-listed oil and gas producers in nine days, underlining the heavy toll the COVID-19 pandemic is taking on one of the country's biggest export industries.

The damage includes a fourth impairment on the value of Santos' 30 per cent stake in the GLNG project in Queensland, which has never produced at full capacity.

The hefty reductions in book values of LNG assets on both sides of the country come on top of billions of dollars of write-downs also announced by multinationals such as Shell on their Australian portfolios.

The latest impairment is one of several at the GLNG project in Queensland, which has never operated at full capacity. *AFR*

They are being driven by moves by producers to slash assumptions for future oil and gas prices as the shock of the coronavirus crisis forces not just a rethink of the immediate softer market but of the longer-term prospects for energy demand.

Woodside Petroleum last week cut the carrying value of its producing LNG plants in Western Australia and its oil assets by more than $US5 billion before tax, and Origin Energy wrote down the value of its Queensland LNG project interest last week, by up to $770 million.

Oil Search has also trimmed the value of its exploration interests in Papua New Guinea and Alaska, while Shell took large write-downs on its QCLNG venture in Queensland and its Prelude floating LNG plant off Western Australia.

Key oil industry 2020 write-downs

Date	Company	Write-downs (pre-tax)	Affected assets	New long-term Brent oil price (real, $US/barrel)
Jul 21	Santos	$US700m-$US800m	GLNG; exploration	62.50
Jul 15	Origin Energy	$720m-$770m	APLNG	60.00
Jul 14	Woodside Energy	$US5.27bn	Pluto LNG; North West Shelf; Wheatstone LNG; oil fields	65.00
Jul 13	Oil Search	$US360m-$US400m	PNG, Alaska exploration; PNG power plant	Not disclosed
Jul 7	ENI	€2.8b	Upstream assets; refining	60.00
Jun 30	Royal Dutch Shell	$US20b-$US27b	QGC, Prelude LNG; upstream assets; refining	60.00
Jun 17	BP	$US13b-$US17.5b*	Oil and gas properties; exploration	55.00

* Post-tax

SOURCE: FINANCIAL REVIEW

The impairments come as [Santos is fighting to get planning approval for its $3.6 billion Narrabri coal seam gas project] in northern NSW in the face of multiple interest groups worried about potential environmental harm and highlighting the risk of "stranded" investments if the world moves more rapidly away from fossil fuels.

Australasian Centre for Corporate Responsibility director Dan Gocher said the Santos write-downs were evidence that oil and gas assets were already being stranded.

"Santos must see the writing on the wall and abandon the Narrabri project before burning any more shareholder capital," he said.

The GLNG project will suffer a reduction in its valuation of between $US640 million and $US700 million before tax, on top of impairments in 2016 and 2017 that totalled more than $US2.7 billion.

A further amount of between $US60 million and $US100 million would be written down in the first-half results on exploration interests, mostly in central Australia, Santos advised.

Santos is now anticipating long-term oil prices will average $US62.50 a barrel in real 2020 terms, just lower than the figure now used by Woodside but still higher than some major European producers such as BP, which has cut its assumption to $US55. The Australian company assumes Brent prices this year of $US45 a barrel, rising gradually over the next four years to 2024 to its longer-term assumption.

'Strong candidate for write-down'

RBC Capital Markets analyst Gordon Ramsay said GLNG "was a strong candidate for a write-down since it has never produced to its nameplate capacity of 7.8 million tonnes a year".

RBC has a valuation on Santos's GLNG interest of $4.5 billion, or $2.17 a share.

The latest impairment will increase Santos' gearing by about 1.5 per cent, but the company said its debt covenants "are not under threat at current oil prices for a number of years".

Chief executive Kevin Gallagher emphasised the action Santos has taken since the oil price dropped in March, including cutting capital expenditure and operating costs, and lowering the oil price threshold at which operations break even on cash flow to $US25 a barrel for this year.

He said those measures saw Santos generate more than $US430 million in free cash flow in the June half of 2020, despite lower prices.

Santos is due to release its June quarter sales figures on Thursday.

Separately, Oil Search posted a 26 per cent dive in sales in the June quarter from the first three months of the year to $US266.2 million, with the average price it got for its oil more than halving. Sales for the first half dipped 19 per cent to $US625.6 million.

Oil Search has advised it will cut its global workforce – predominantly in PNG and Alaska – by 34 per cent by the year-end. It raised about $US700 million in fresh equity earlier this year to stave off concerns about its balance sheet.

Output in the June quarter slipped 1 per cent from the March quarter to 7.29 million barrels of oil equivalent, but first-half output still rose 4 per cent.

Analysts described Oil Search's operating performance as "solid", but JPMorgan's Mark Busuttil pointed to lower than expected commodity prices.

Oil Search received an average of $US23.05 a barrel for its oil and condensates in the quarter, less than half the $US49.51 a barrel received in the March quarter. Its average price for LNG and gas slipped to $US7.34 per million British thermal units from $US9.08.

"On the positive side, the company reiterated full-year production guidance while lowering the high end of operating cost guidance," Mr Busuttil said.