

**Smelling Salts; An Indian group's investment in an Australian ammonia factory has been a lesson in boom-time costs. Next stop: Papua New Guinea.**

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When Pankaj Oswal started building one of the world's biggest ammonia factories in Australia in 2001, he was hailed as India's answer to China's domination of Australian resources development. But rather than celebrate the completion of the \$575 million Burrup Fertilisers plant earlier this year, Oswal, who is Burrup's chairman, has been left lamenting Australia's hothouse economy. There, demand from India and China is producing sharply rising costs and a chronic labor shortage.

For Oswal the dream of blazing a trade trail between India and Australia has turned so sour that the next big investment by his high-profile Indian family, he says, will be a \$500 million factory, also making ammonia (and urea) for fertilizer production, in Papua New Guinea.

"We would love to do the new project in Australia," Oswal says in his Perth office. "But the gas price here is too high, and labor costs have risen too rapidly. There's also an issue with the exchange rate, which has risen from 60 [U.S.] cents when we started Burrup Fertilisers to 76 cents today."

Natural gas, from vast fields along Australia's remote northwest coast in spots like the Burrup, is a basic ingredient in ammonia. That pungent product is a combination of hydrogen (extracted from natural gas) and nitrogen (from air). It's exported in liquid form (after being chilled to minus 33 degrees Celsius) to fertilizer plants, mainly in Asia. Successive Australian governments have been seeking investments like this for more than 30 years; so far Burrup is the only gas-to-liquids investment. (A different application, liquefied natural gas, is exported for electricity production in such countries as Japan and China.)

"The major attraction in coming to Australia was the gas price," Oswal says. "Since 2001 it has risen threefold. We also suffered a delay of about nine months in construction, the unions gave us a horrid time, and the overall cost blew out by 20%. [Oswal doesn't give specific financials.] The price we're being offered in Papua New Guinea today is far more competitive than current prices in Australia."

Oswal declines to give specific prices because the Papua New Guinea gas supply contract is not yet signed. However, sources close to Burrup Fertilisers say it's negotiating a rate that is close to one-third less.

"The big attractions of Papua New Guinea for us are simple. It's the gas price and the cost of labor. About 70% of the cost of ammonia is the gas, and it's getting too hard to find skilled workers in Australia because of the resources boom," he says.

Over the past year competition for labor in the resource-rich parts of Australia (mainly in the states of Queensland and Western Australia) has driven the unemployment rate down sharply and wages up. The national unemployment rate in August was 4.9%; in Western Australia it dropped to 3.6%. Wages in the mining and oil sector are now the highest of any sector, averaging \$70,000, with specialists paid \$150,000 and more--if they can be found. The Australian government is even considering offering a special one-time payment of \$3,800 to help meet the relocation costs of workers who move to the resource-rich parts of the country.

In backward Papua New Guinea, by contrast, labor costs can be from a third to two-thirds that of Australia, even after skilled workers must be imported from the Philippines and elsewhere. At the same time risks associated with a weaker rule of law are harder to quantify.

In Australia's field, cost blowouts and budget delays are hampering most developments. Woodside Petroleum's \$1.5 billion expansion of its LNG project has suffered a \$320 million, or 20%, increase in costs; BHP Billiton's Ravensthorpe nickel project is expected to cost 50% more than its original \$1 billion budget when completed next year; and fresh budget estimates for Chevron's proposed Gorgon LNG project are expected to show a jump from \$8.5 billion to around \$11 billion when announced later this year.

Pankaj Oswal doesn't have that kind of money to throw around. His family, which has a 55% stake in Burrup, has a troubled business history, largely because of problems with Oswal Chemicals & Fertilizers. The Indian company has posted heavy losses, sold half of its fertilizer capacity and been locked in legal battles with the Indian government, including a recent loss in the Delhi High Court over fertilizer pricing. In April last year the family delisted Oswal Chemicals from the Delhi and Uttar Pradesh stock exchanges.

Other shareholders in Burrup are Yara International, one of the world's biggest fertilizer producers and traders, which has a 30% stake (plus the rights to market all of Burrup's production), and another Indian family, the Rambals, who have a 15% interest but have fallen out with the Oswals. Pankaj Oswal says he no longer speaks with the former managing director of Burrup, Vikas Rambal. For his part, Rambal says that "relations are somewhat strained."

Despite Oswal's criticism of Australia's boom-induced costs, the country's industry minister, Ian Macfarlane, says the Oswal investment is a milestone in Australia's gas-processing industry and a step up in the historically sluggish trade relationship between India and Australia, which amounted to only \$1.5 billion in 2000 before growing to \$6 billion last year.

Oswal says his overall experience in Australia has not been all bad. "We've learned a lot," he says, with a rueful laugh. "Other Indian companies have asked [us] about our experience, and I've said it's good--but not right now. The timing is not correct. It's a boom, costs are going haywire, and the competition is too hot."

Energy sources are top of the shopping list for Indian and Chinese companies; minerals are a major secondary target. Last year saw the listing on the Australian Stock Exchange of Aditya Birla Mineral Resources, a specialist copper-mining company that is ultimately controlled by one of India's biggest companies, Hindalco Industries.

Aditya Birla operates the Nifty and Mount Gordon mines and ranks as the biggest pure copper company on the ASX and fourth-biggest copper producer in Australia. In late July the managing director of Hindalco, Debu Mhattacharya, reportedly told a media conference in Mumbai that Hindalco was sourcing 25% of its copper from mines acquired in Australia over the past two years.

But like the Oswal ammonia investment, Aditya Birla is suffering. It disappointed investors by incurring a loss of \$13 million in the year to Mar. 31. That result was better than the \$18 million loss in 2005, but both poor results came at a time of high copper prices.

Management of Aditya Birla, which declined several requests to speak with FORBES ASIA, blamed "increased cost pressures" and "high staff turnover and skill shortages" in a presentation to investors following the latest loss. On Sept. 6 the company reported further problems, this time the temporary suspension of mining in part of its Mount Gordon mine, which may restrict copper production this year.

Macfarlane admits that part of the problem encountered by Indian investors is related to the skills shortage. "We've got projects in gas and minerals that are basically almost queuing to get labor," he says. "We've seen the escalation in labor rates particularly up on the Burrup."

When asked whether Australia could handle the rising demand for resources from India and China at the same time, Macfarlane hesitates: "I think it's probably a bit early to decide that. Most people seem to agree that India will become a huge market, and it's likely that that will happen but not in the near term."