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Macquarie: WPL - LNG’s Golden Future

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Trading Pick of the Day

It’s no secret that Woodside Petroleum (WPL) is aggressively developing its capacity as an LNG producer through its flag-ship Pluto field. But is this strategy a sound one? Should it be betting a significant amount of its future earnings stream on Liquified Natural Gas (LNG). In today’s story, Macquarie Research Equities (MRE) investigates!

The LNG business is dynamic and is changing rapidly. At the turn of the century, there was a definite buyer’s market for LNG, but we are today undoubtedly in a seller’s market. There have been a number of reasons for the change – the recovery of LNG consuming nations from the Asian Financial Crisis of the late 1990s, the rise in oil prices from $25/bbl to $60+/bbl, and a realisation of the need to arrest and reverse carbon dioxide emissions and environmental damage.

All markets are now paying for gas. The Chinese government and state-owned enterprise LNG project sponsors typically object to current ‘high’ international LNG prices, but MRE view this as a negotiating tactic. The retail price for industrial and commercial gas users in many of China’s provinces is already over US$10/GJ. While the Guangdong and Fujian contracts were originally signed in 2002, China has clearly now realised that the market dynamics have changed, and that higher prices are required. CNOOC and Malaysian LNG (MLNG) recently agreed an LNG supply deal for Shanghai with 2008/9 delivery, at a plateau rate of 3mtpa, reportedly at $US6.34/mmBtu FOB. In fact, MRE believe that new LNG contracts currently being negotiated are pushing the price ceiling higher and higher, with at least one contract recently agreed without a ceiling from Qatar. At US$55–60/bbl oil, the fully correlated LNG price on a one-for-one basis would be towards US$9/bbl (CIF).

Winning first mover advantage. With this demand outlook, MRE see the most aggressive developer as the most likely winner, and in this light, Woodside’s (WPL) Pluto development is a clear standout. With discovery in 2005 and a target start-up date by end 2010, its development timeline is certainly aggressive. Further, at its recent full-year results announcement at the end of February, management again highlighted their focus on ensuring the Pluto development remains on track. MRE continue to highlight the importance of this asset to the long-term value of WPL.

MRE reiterate their outperform recommendation and 12-month price target of $40.53.

Traders looking for maximum exposure to short-term movements in the WPL share price should consider the following equity warrants for a high-risk, high-return strategy.

Investors and traders looking for short to medium-term leveraged exposure to the WPL share price should consider Macquarie Instalments for a higher risk, higher return alternative to direct share investment.

Long term, more conservative investors looking for a simple, "set and forget" investment should consider the Self Funding Instalments over WPL. SFI's are moderately geared, have no annual resets and a maturity date in up to ten years.