

# THE FAIRBANKS PIPELINE COMPANY

*AN ALASKAN SOLUTION*

**Best Value of ANS Gas**

**The Story of Exportations (AGIA & AGDC) and In-State Utilization (FPC)**

**1/2/11**

## The Views

- 1 There seems to be only one view emanating from our administration on how to extricate the best value from ANS gas. This is the AGIA big pipe or the AGDC medium pipe view, where the availability of this affordable gas to Alaskans is contingent on an exportation pipeline , if and when installed. Both these schemes are all about cash flows, or as this analysis will demonstrate, short - term profits
- 2 There is another view that Alaskans should consider. It is the prioritization of ANS gas for in-State use to cut Alaskan energy costs in half by 2014. This option can also:
  - Make Alaskan residents and companies owners of the pipeline serving their needs. As opposed to the big pipeline, this sensibly sized pipeline does not have to wait for gas prices to be feasible, thanks to the exorbitant prices we pay for our energy today (using the term thanks loosely)
  - Through ownership of the pipeline, Alaskan residents and companies can also receive annual dividends of \$11.07 on every \$100 share purchased
  - Alaskans who do not choose to invest in the Arctic Fox Pipeline will also benefit because FPC plans to give the Alaska Permanent Fund 515,520 shares in exchange for pipeline easements along the Dalton and Elliot Highway Corridors , project permits, and publicly owned geologic and geophysical data
  - Lest we not forget, this option also leaves gas in the ground for our children's use

That is why FPC has named our pipeline the Arctic Fox. While it is small and nimble, it is also smart and quick. Read on to see the details and go through some easy math with us so you can cast your own judgment on these two diametrically opposed views

## The AGIA or AGDC Centric View – Focus on Exports

AGIA is all about obtaining large cash flows into State coffers as quickly as possible. Exporting ANS gas at high volumes (4.5 Bcf/day) produces relatively large cash flows at nearly any exported gas price because almost any price over these huge gas volumes yields lots of dollars.

For example:

4.5 billion cubic feet per day equals 4.5 million units of trade because gas is priced and traded in 1000 cubic foot units (mcf). So... under AGIA's big pipe, we would be exporting 4.5 million mcf/day or 1,642 million mcf per year.

More easy math:

The State makes about 12% on the value of gas produced (and exported in either the AGIA or AGDC case) unless the Administration enacts further cuts in State revenues. Therefore, when the day comes that gas producers can make a dollar on every mcf they produce and export, the State will retain 12 cents on every mcf exported. This does not seem like much per unit, but when multiplied against 4.5 million mcf/day, it adds up quickly.

$$12 \text{ cents} \times 1,642 \text{ million mcf/year} = \$197,040,000/\text{per year}$$

This is a nice cash flow, but how does this transpose into value for Alaskans?

By the way, the Administration is sitting on a \$12.3 Billion Dollar Constitutional Budget Reserve today  
This budget surplus is about the same as California's entire budget deficit today

The math stays easy and the story becomes more interesting, so read on.

## Treating the Myopic Disorder

We can all agree that the addition of \$197 million per year to the State's already fat checkbook seems attractive. However, our purpose is to weigh the value of these deposits into the State's checkbook along with our own thinner checkbooks because in either case, it's value left in Alaska

It just so happens that in the Interior of Alaska, 1/6<sup>th</sup> of our State's population is paying at least double what they could be paying for energy served by ANS gas

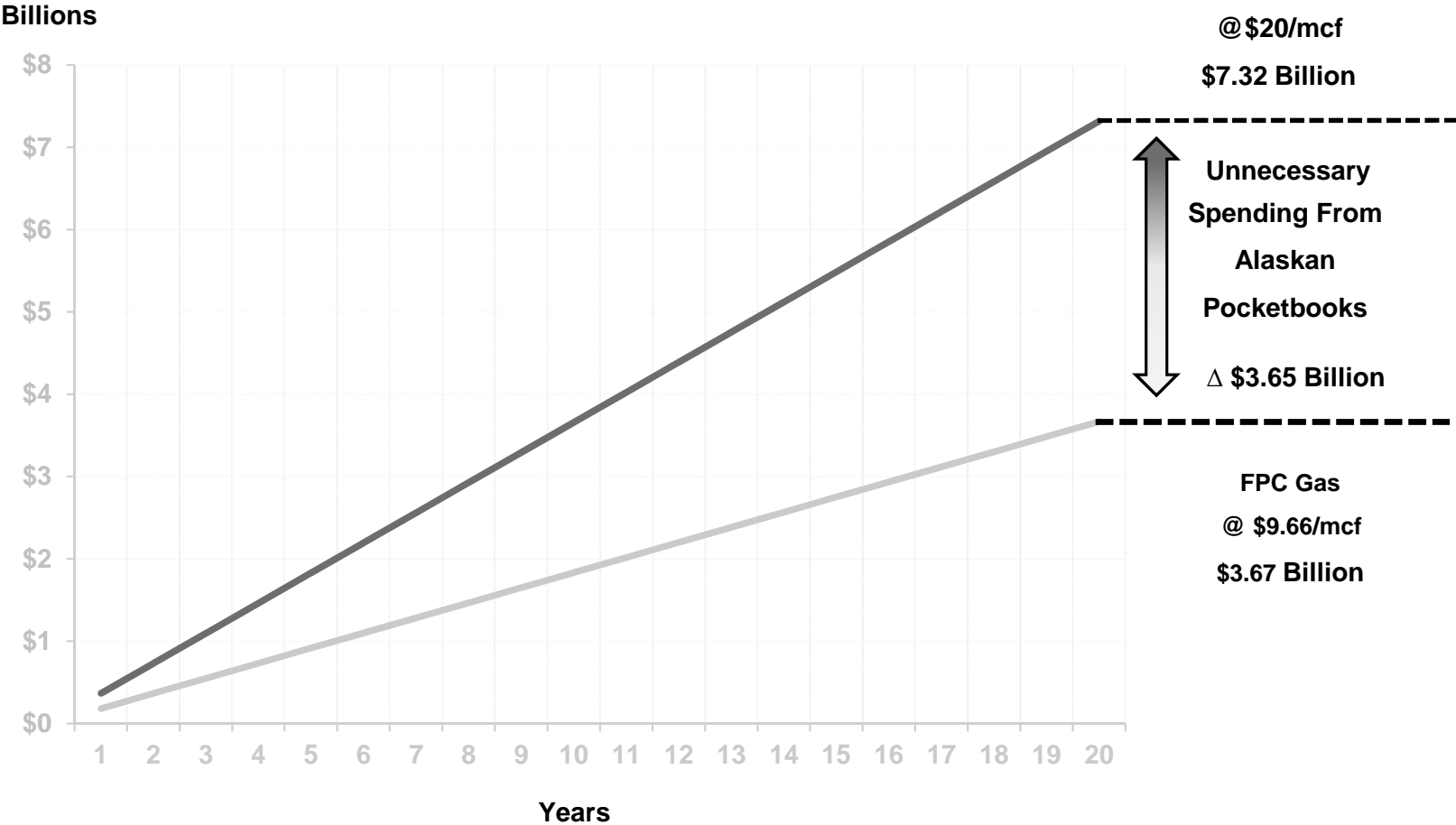
The next two slides show what Interior Alaskans are now paying for their energy versus what they could be paying if served by the Arctic Fox Pipeline under two scenarios:

Scenario One: FPC's current gas nominations received from Interior Load Centers such as GVEA, the Refineries, FNG, etc. This is 19 Bcf per year, roughly four days of gas the big pipe would be exporting if it was possible, which it is not - because the world is experiencing a glut of cheap gas supplies

Scenario Two: This shows 30 Bcf of gas delivered to the Interior, which makes economic sense because it lowers the cost of gas the Arctic Fox Pipeline will deliver from \$9.66/mcf to \$7.65/mcf. Because energy prices in the Interior are over \$20/mcf when crude goes over \$87/Bbl, this drops energy prices from half at 19 Bcf/yr to a third at 30 Bcf/yr. Keep in mind that crude prices are over \$90 today and expected to rise beyond \$130/Bbl in the foreseeable future

# AGIA & AGDC - Sell the Cows and Burn Down the Barn

Scenario One, 12" North Slope to Interior Pipeline Moving 19 Bcf/Year



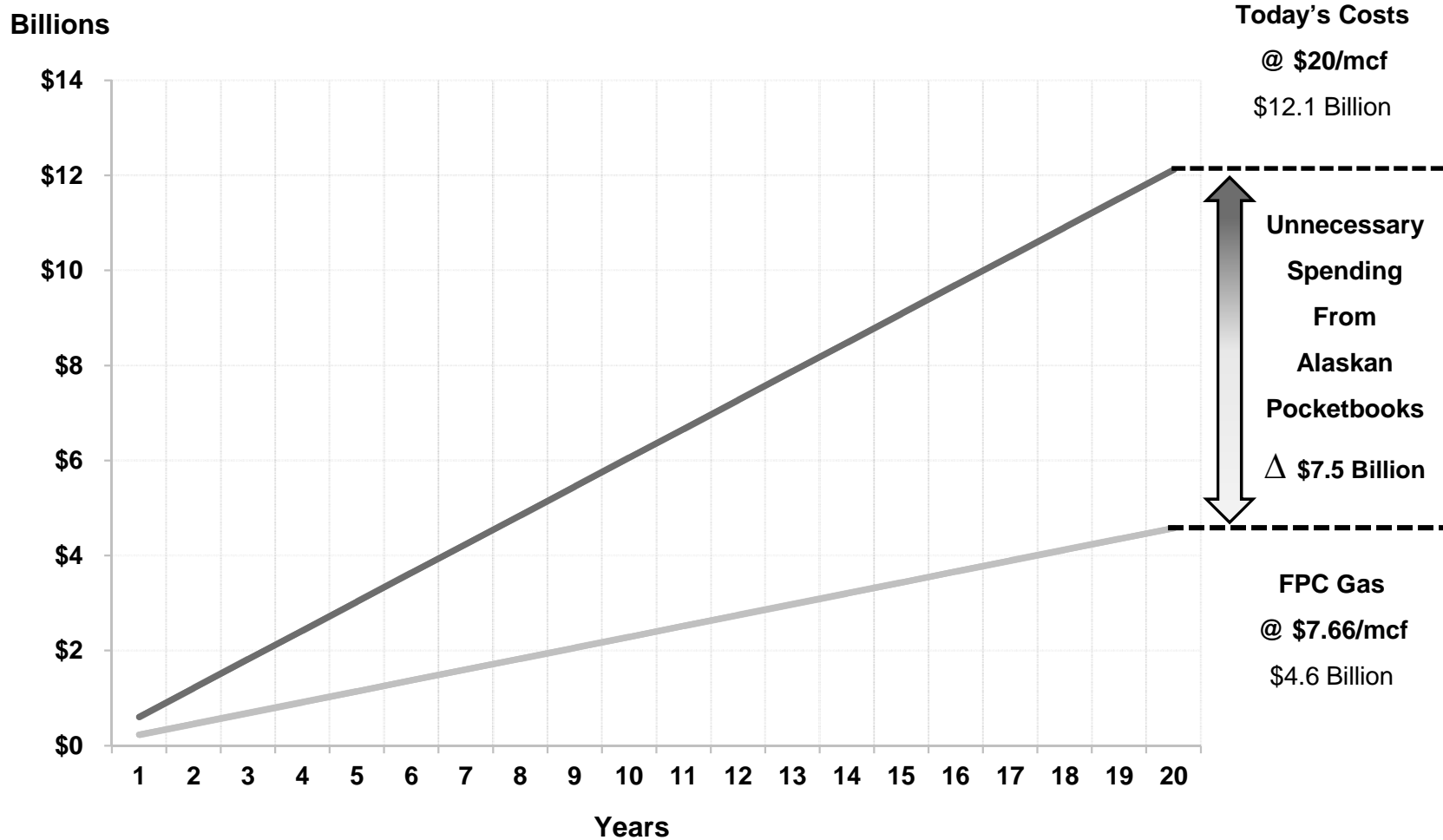
Today's Costs  
@\$20/mcf  
\$7.32 Billion

Unnecessary  
Spending From  
Alaskan  
Pocketbooks  
Δ \$3.65 Billion

FPC Gas  
@ \$9.66/mcf  
\$3.67 Billion

# AGIA & AGDC - Sell the Cows and Burn Down the Barn

Scenario Two, 12" North Slope to Interior Pipeline Moving 30 Bcf/Year



## AGIA & AGDC's Quick Profits on Exportations

What did the previous two slides show us?

Scenario One at 19 Bcf/yr:

If not served by the Arctic Fox Pipeline, Alaskans will pay \$3.65 Billion more for their energy requirements in twenty years. Once again, the easy math says \$3.65 Billion/20 years is roughly \$183 million per year

Scenario Two at 30 Bcf/yr:

Because we are replacing a higher volume of expensive fuels with cheaper gas (30 Bcf/yr vs. 19 Bcf/yr energy equivalent) and because when you move more gas volumes through a pipeline, its transportation costs per unit drops (from \$5.44/mcf at 19 Bcf/yr to \$3.44/mcf at 30 Bcf), the savings to the Interior increase from \$3.65 Billion to \$7.5 Billion over 20 years or roughly, \$375 million per year.

A brief review is in order before we get to the punch line:

The quick AGIA dollars retained in State when and if the big pipe comes \$197 million per year

The savings to Alaskans through the Arctic Fox Pipeline	@ 19 Bcf/yr	\$183 million per year
<i>(based on \$87/Bbl crude)</i>	@ 30 Bcf/yr	\$375 million per year

Is this the end of the story you ask?

Not really – read on because the math gets easier and the drama is about to GROW!

## After the Cows and Barn are Gone, Comes the Slight of Hand

We reviewed the dollars on the last slide, but in fact we started this presentation with the grand numbers the big AGIA pipe will ship south of our borders. Let's now compare the volumes of gas this big pipe will export every day versus what the Arctic Fox will transport to Alaskans:

The big pipe dreams	4.5 Bcf/day or 1630 Bcf/year
The little, but very sensible Arctic Fox	19 Bcf/yr or 30 Bcf/year

Now let's be kind to the big AGIA pipe dream by assuming that someday we will run a pipe from Livengood to the Cook Inlet and deplete our gas wealth on the North Slope at a quicker rate than the Interior with its paltry numbers

If we take the Interior's larger number of 30 Bcf/yr and add it to the Cook Inlet's current non-exported volumes of 72 Bcf/yr, we get 102 Bcf/yr. The North Slope has 34Tcf – 37 Tcf of proven gas reserves

Because the fox is kind, we will use the larger number of 37 Tcf. Let's now look at how we tear through this gas wealth and erode our legacy to our children:

The AGIA big pipe dream	At 1,630 Bcf per year, it's all gone in 22.5 years
The kind Arctic Fox Pipeline	At 102 Bcf per year, it leaves 32.5 Tcf in the ground after 22.5 years

End of story you ask? Not at all, read on to see what lies under the shells being shuffled on the table



## AGIA & AGDC - The Shell Game

Let's lighten up on our light math and look at the moving shells on the carnival table using a little logic

Why does any pipe work? Because the gas it moves to markets has value. Without a pipe gas only has latent value, not marketable value because it sits in the ground and the cash register never jingles

So with either pipe, stranded North Slope gas can be transformed from latent to marketable value

Like money, value is what value reaps. The question now becomes who reaps?  
Let's review the value to Alaskans again:

The quick and dirty AGIA dollars retained through royalties		\$197 million per year
---	--	------------------------

The savings to Alaskans through the Arctic Fox Pipeline	@ 19 Bcf/yr	\$183 million per year
	@ 30 Bcf/yr	\$375 million per year

Its easy to see that the Arctic Fox Pipeline provides equal or greater value to Alaskans than AGIA.

What about the Fox's kind work in providing Cook Inlet the prospect of containing their future cost by bringing North Slope gas 418 miles closer to Anchorage? Remember, this would grow Alaska's utilization of North Slope gas to 102 Bcf/yr.

Let's just skip the math for now and stay with logic because you will soon see that it really does not matter.

Really you ask? Read on

## The Shell Game

### So where is the Pearl?

For the State to obtain its 12 cent royalty, the price of gas in common markets needs to climb to at least \$12 dollars to pay back the investment of installing the pipe dream to markets priced at \$4.50 today.

Because there are no gas markets at our border, more than the 730 miles of gas pipeline in our State costing \$24 Billion would need to be installed to reach gas markets ( again, priced at \$4.50 today)

While there are already interconnections from Canada to the Midwest markets, these lines are full. Another 1500 miles of pipeline would need to be installed or alternatively a very large LNG plant would need to be installed at tidewater. Let's call it another \$25 Billion either way. This brings the investment total to roughly \$50 billion.

The companies who invested in TAPS got their investment back in three years. Let's be kind to AGIA and assume that they would be willing to undertake a capital risk of six times that of TAPS for a twenty year pay back. This requires a gas price of \$11.26/mcf. We said \$12 above, but we'll just leave the State's royalty take at \$1.00/mcf instead of 74 cents because again, you will soon see that it does not really make any difference

## The Shell Game Continues

We have already deduced that with either pipe, ANS gas is transformed from latent to marketable value. Are there any other metrics we can now apply to our logical argument? Off course there are.

These metrics are called current and future marketable value. The current value is gas moving through the pipe and the future value is gas in the ground. With either pipe the cash register is now in place and singing. Now we need to introduce yet another factor.

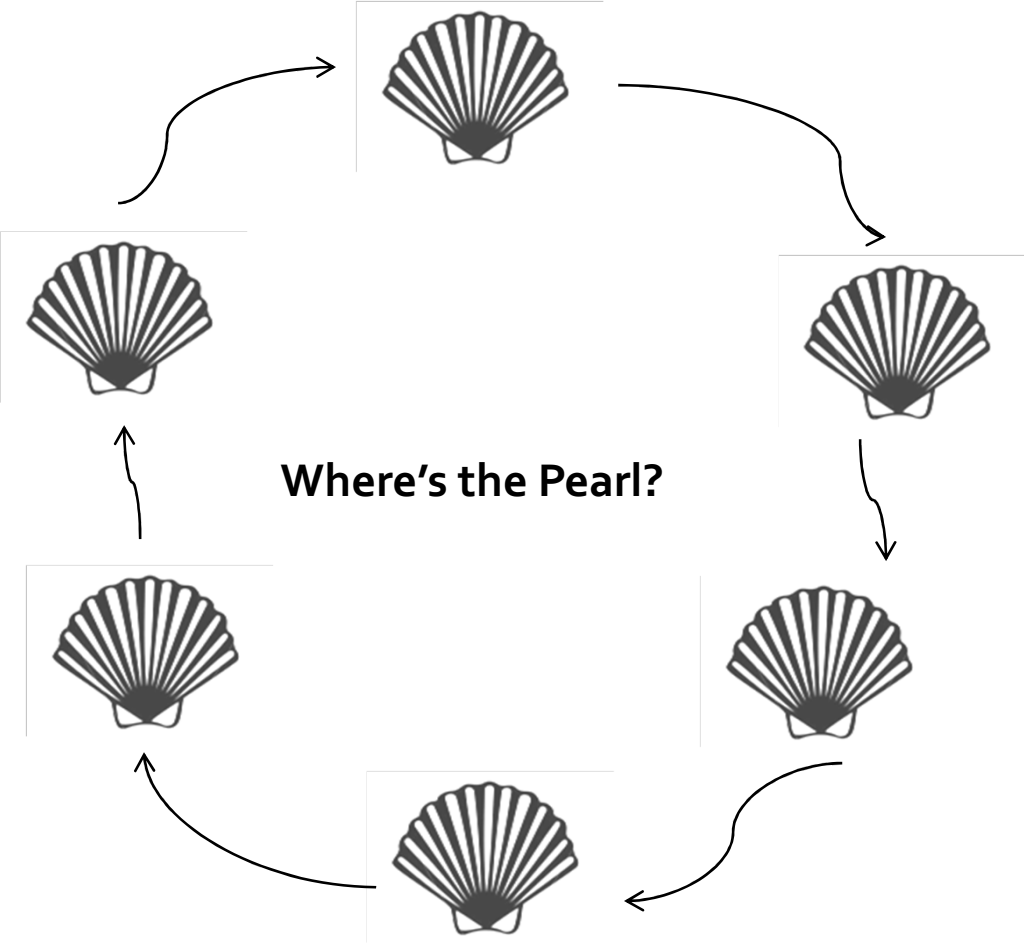
As any good storekeeper knows, this factor is called inventory. Back to simple math:

We know that in 22.5 years, the AGIA pipe dream will deplete our State's inventory of proven North Slope gas reserves to zero. After 35 years, the kind Arctic Fox will leave 32.5 Tcf in the ground for our children and future generations if alternative energy sources are not in place.

What about now? We keep about the same amount in our worn pockets as the State will make in Royalties. So, let's be kind to our children like the Fox because if we are kind, the Fox will reward us by improving our permanent fund dividends. He will also let us invest a few dollars in the pipeline and pay us \$11.07 every year for every \$100 share we purchase.

So where is the Pearl? Next slide please

**Exportations Versus Prioritization of In State Use**  
**The Shells and the Money Move Fast**



# We Found It – Which Shell Did You Choose?

We lost track, but the small, nimble and smart Arctic Fox found the pearl and guess what?  
He stands ready to share the pearl with all Alaskans

## Exportations

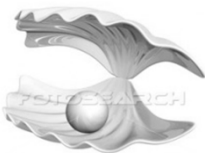


22.5 years of State Royalties escalating 2% per year from \$1.00/mcf to \$10/mcf	\$23.04 Billion
22.5 years of energy savings to Alaskans if and when big line is built	\$0.130 Billion
22.5 years of earning through ownership in the BIG pipeline	\$0.00
Gas inventory left in the ground for our children	<u>\$0.00</u>

Assuming start up in 2027 and gas depletion in 2049 (22.5 years of operation)  
Gas market value at start up - \$14.86/mcf  
Gas market value escalating 2% per year to \$22.53 on its last year of operation

Value to Alaskans: **\$23 billion**

## In-State Prioritization

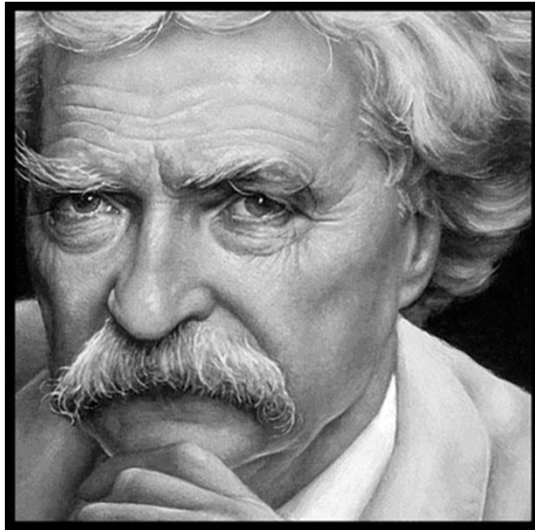


35.5 years of State Royalties escalating 2% per year from \$1.00/mcf to \$11/mcf	\$1.48 Billion
35.5 years of energy savings to Alaskans (102 Bcf/yr)	\$13.80Billion
35.5 years of earning through ownership in the Arctic Fox Pipeline	\$10.43Billion
Gas inventory left in the ground for our children after 35.5 years	<u>\$753 Billion</u>

Assuming start up in 2014 and 35 years of operation  
33.5 Tcf gas left after 35 years, so it keeps running for our children  
Same gas valuation basis as above (2% escalation per year)

Value to Alaskans: **\$778 Billion**

“I find that, as a rule, when a thing is a wonder to us it is not because of what we see in it, but because of what others have seen in it. We get almost all our wonders at second hand...By and by you sober down, and then you perceive that you have been drunk on the smell of somebody else's cork”



“I was seldom able to see an opportunity until it has ceased to be one”