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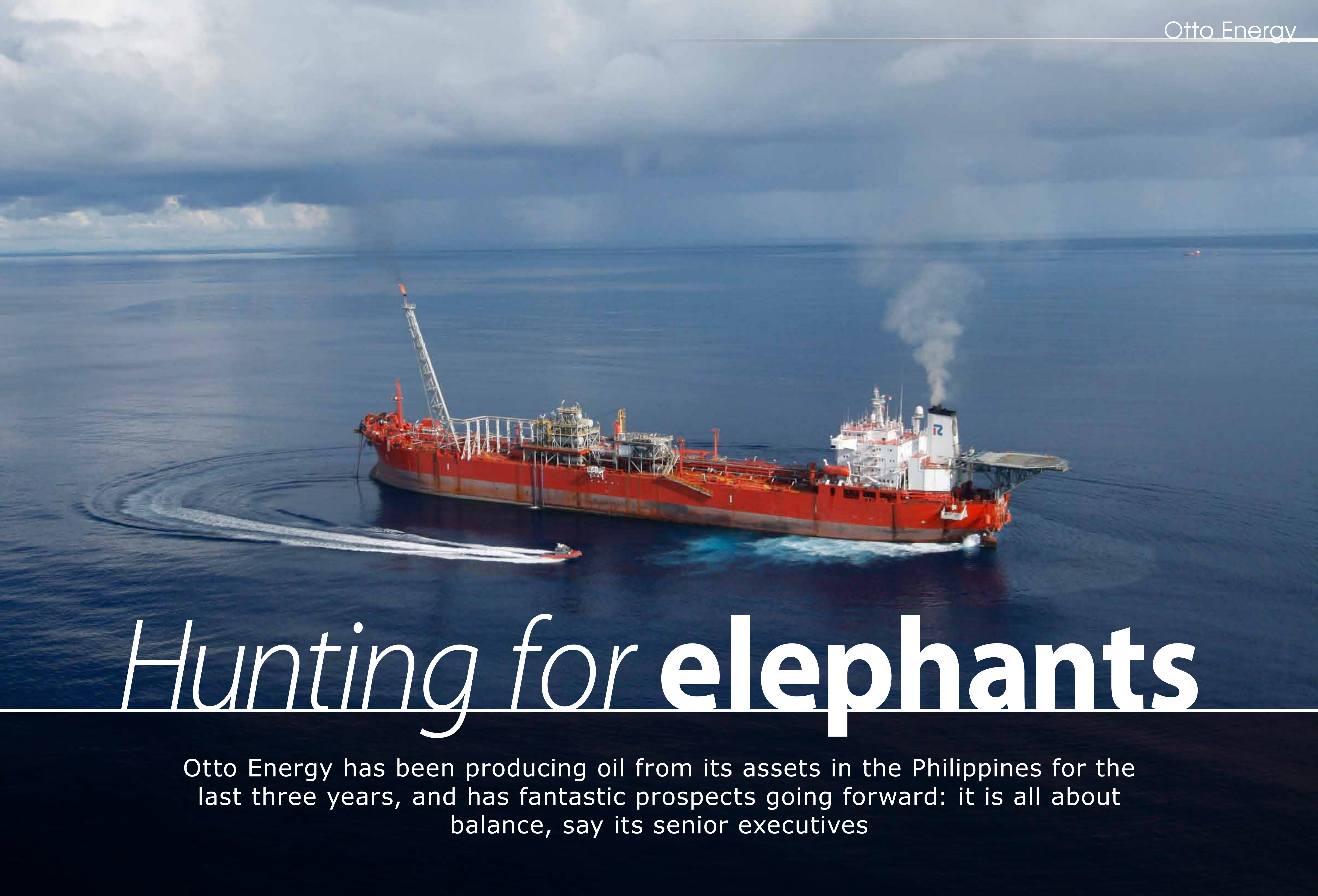

Hunting for **elephants**

Otto Energy has been producing oil from its assets in the Philippines for the last three years, and has fantastic prospects going forward: it is all about balance, say its senior executives

When it listed on the Australian Stock Exchange back in 2004, Perth-based Otto energy was purely in the business of oil and gas exploration, putting together a portfolio of properties in areas it thought had potential, and focusing on the Philippines. In 2007 it graduated into being a production company too, when it bought a share in the Galoc Production Company (GPC). Today it is in the enviable position of having strong cash flow from its initial producing wells, firm plans to increase that, prospects of considerably more, and a credible strategy to extend its successful business model into other parts of the world.

There's a 1,000 kilometre-long oil and gas 'fairway' that runs from the north-western coast of Malaysia all the way past the Philippines island of Palawan and up to Mindoro to the south of Manila and the main island Luzon—and it is relatively underexplored. Compared to the other countries that border the South China Sea/West Philippine Sea—Vietnam, Malaysia, Indonesia and China itself—few of the major players have come in yet, says acting CEO Matthew Allen, and the waters off the Philippines were really only re-opened for business in the late 1990s, though interest is rising now.

Otto has four active projects, or service contracts, with the Philippines Department of Energy. The most advanced is the Galoc field, being developed by a joint venture in which GPC has a one-third stake. GPC is now wholly owned by Otto Energy, following the purchase of the majority shareholding previously held by

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Vitol Group. GPC was set up as a Vitol subsidiary in 2005; however, as time went by and Otto developed, the field became strategically much more important to Otto, for whom it represented a very attractive opportunity, and less so to Vitol as the latter turned its attention to interests it has in West Africa.

Galoc was the launching pad for Otto in the Philippines and to date the two wells that comprise Phase I have yielded more than eight million barrels of oil. “There’s good follow-up potential there,” says Otto’s Philippines country manager, Ross Prasser. “The Galoc field has produced well since start-up, and that gives us the encouragement to study potential additional wells into untapped parts of the field. We have just launched into a pre-investment study on Galoc Phase II that will be going on over the next few months.”

The front-end engineering and design (FEED) process will decide the number and location of the additional wells that will be drilled and the infrastructure that will be needed, including wellheads, flow-lines and umbilical lines. Final project approval is scheduled for mid-2012, and Otto hopes to start drilling in 2013. As a preliminary, the Rubicon Intrepid FPSO (floating production, storage and offloading) vessel is having its mooring and riser system upgraded.

Meanwhile a team has been assembled in Perth to undertake the FEED study. For Otto, it is a really exciting and indeed essential project that will take investment of around $140 million. “We now do most of the work ourselves, which demonstrates Otto’s increasing capability as an operator through the development and production phases,” says Prasser.

To avoid any doubt as to precisely what is down there and where it is, a seismic survey is now in progress over 71 square miles of the Galoc field. This highly specialised work is being carried out by China Oilfield Services Limited and is a bit like a gargantuan ultrasound scan that can create a map of underground resources. "It gives us much better imaging of the reservoir and a better idea of where the sweet spots are," says Prasser. "That will help us in positioning additional wells."

Further south, off the island of Palawan, Otto has a one third interest in Service Contract 55, covering nearly 10,000 square kilometres with significant hydrocarbon potential. The Philippines government is extremely keen on the possibility of discovering further large deposits of gas to complement the Malampaya project operated by Shell. The holy grail is to discover the next multi-TCF (trillion cubic foot) gas deposit in the Philippines. "We are looking for the elephants in this block," says Allen.

But it lies in deep water, between 400 and 2,000 metres down. "This block needs a competent deep water operator and BHP Billiton, which operates in the deepwater Gulf of Mexico and Australia, has the experience to drill these wells," says Allen. BHP Billiton is bringing in a lot of money and expertise, funding wells that will cost around $70 million each, and the participation of a major oil and gas player like BHP Billiton in this block reinforces the prospectivity of the area. "A major player of the calibre of BHP Billiton supports our view of the Service Contract 55 area as a major unexplored play with high potential, in fact one of the last underexplored areas on the South China Sea/West Philippine Sea rim." A rig has been secured, and drilling will start in the second quarter of 2012.

With the BHP Billiton farm-in agreement and the Galoc acquisition, 2011 has been a very significant, indeed critical, year for Otto Energy. It is clearly going to be very busy in 2012 too, with two other projects at an advanced pre-drilling stage in the Philippines, including a very exciting onshore hydrocarbon prospect on Leyte that is due for seismic follow-up next year.

One of the great advantages for an Australian company working in the Philippines is that it is geographically close, in the same time zone even. But Otto is also looking further afield, for opportunities in relatively undeveloped regions. A promising area is the Rift Valley of East Africa, says Allen: "We are looking for onshore opportunities to balance our offshore portfolio in the Philippines—we have been engaging with governments and potential joint venture partners over the last year, and maturing various opportunities."

Balance is the key word, and Otto Energy has it in spades. It has cash flow from existing operations, interests in both oil and gas, is developing geographical spread—and it has those elephants in clear view. That's a picture that investors will find attractive as the world economic horrors abate and they start to look more kindly on medium-risk, high return prospects. **www.ottoenergy.com** ■

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