

On June 28, 2002, Lord **John Browne**, Group Chief Executive, BP, addressed a large combined audience of the Anchorage Chamber of Commerce, Alliance and Resource Development Council for Alaska on a variety of oil and gas policy issues, including those related to an Alaska gas pipeline. The meeting convened in the Sheraton Anchorage Hotel's Howard Rock Ballroom.

We are grateful to **Ronnie W. Chappell** of BP for providing this text to *Northern Gas Pipelines* for use of our readers. We changed the format to .pdf and added an introduction for reader convenience.

Ladies and Gentlemen.

Good morning.

It's great to be back in Alaska, and it's very good to see so many of you here, including so many old friends and colleagues.

It is just 33 years ago this autumn since I first came here - as a very young graduate who'd just joined BP. It was my first job.

This is where I learnt about the reality of the oil industry - the real challenge of developing resources in complex circumstances, the challenge of bringing those resources to market - and the challenge of working with a vast range of people - all in pursuit of a common objective.

And there's nowhere better to learn. Because this is a place full of great people who have mastered reality. A very diverse group of people who have overcome every challenge ... and come out on top because they have understood that by working together, what appears impossible can be made achievable and real.

That grounding in reality was very important for me - and it has always stayed with me.

It has shaped how I look at people and ideas and projects and investment proposals.

Because business has to be about reality or it fails.

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And that was my first thought as I was preparing to come back here.

What is the reality now?

What are the possibilities for the future?

And what will it take from us, or anyone else, to turn those possibilities into a new reality?

What action is necessary, and what real consequences will follow?

I put that heavy stress on reality because I think there have been times when the aspiration has gotten too far ahead of what can be achieved.

The track record of forecasting here isn't great. And that includes our track record.

I can remember - because in some cases I was directly involved - a number of occasions when that was the case.

The idea that there would be no decline in oil production, that there would be a great new wave of exploration activity, that Pt Thomson or Northstar was the first of a significant wave of major new fields, that oil prices were going to stay at more than \$30 a barrel ... and so on.

People thought about what they wanted to happen ... but the aspirations outstripped the facts.

At the same time, the industry here has made some mistakes.

Not just environmental and operational mistakes, but also mistakes about establishing priorities. Not being clear about what we were doing and why, and not always explaining the economic realities to staff and to Alaska's citizens.

And the result of all this is that there have been some negative surprises ... and some false dawns.

Those gaps between the promise and the delivery have occasionally created a climate of disappointment - a sense of underachievement - which takes away from what has actually been achieved here - both by the industry and by Alaska as a whole ...

They diminish the pride which there should be in those achievements.

The achievement of a sustained and very successful operating oil business. The achievement of building a permanent fund. And the achievement of building a significant city here in Anchorage and a great civic community.

Those negative surprises and false dawns also discount the credibility of what can still be achieved ... because they've eroded trust.

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So to focus on reality is neither to be optimistic nor pessimistic.

Optimism and pessimism don't have much place in business. I prefer the view of a great American President who said that he was neither optimistic nor pessimistic - he was determined.

So what is the reality?

Nearly 14 billion barrels of oil have been produced on the North Slope of Alaska in the last 25 years.

A strong infrastructure is in place which links Alaska into the world market.

There are, on the North Slope according to the USGS, a total of 5 billion barrels of booked oil reserves, another 9 billion barrels of oil resources not yet booked and some 13 billion barrels yet to be found.

We in BP have nearly 2 billion barrels of proven oil reserves discovered and remaining to be produced in fields already in production. In addition, we have over half a billion barrels of undeveloped oil reserves which we believe can be developed, and some 3 billion barrels of oil resources which we don't yet know how to develop competitively.

There is, on the same USGS figures, a total of 35 trillion cubic feet of natural gas discovered, and perhaps another 100 trillion cubic feet still to be found. BP holds about a quarter of the discovered volume. What is at issue is whether any of that gas can be developed competitively.

Those are the first elements of reality.

The second point is that there are plentiful resources of oil and gas in the world.

On our latest estimates, over 1,000 billion barrels of oil and nearly 5,500 trillion cubic feet of gas - and those figures are just of proven reserves.

Those resources are concentrated in a number of areas, but by no means exclusively in the Middle East.

Last year the U.S. imported nearly 12 billion barrels of oil, and net imports accounted for 55 per cent of its consumption - but that oil came from 60 different countries around the world. No one country supplied more than 15 per cent.

And that diversity of potential sources of supply is being sustained. The Caspian and West Africa and, of course, the deep water Gulf of Mexico are all set to grow in importance and can supply the growth in demand in the world market for many years to come.

Of course, it must be right to say that having domestic production of energy enhances security ... but I don't believe it is realistic to expect domestic production to be supported regardless of the costs. To do so would undermine the competitiveness of the whole economy.

The point of saying that is to demonstrate the reality - which is that Alaskan resources have to be able to compete at the point of consumption in the global market.

The end user, the consumer who burns the oil, cannot and does not differentiate as to where the oil comes from.

And the same is true for gas. There is no shortage of potential gas supplies.

In Australia, in Indonesia, in Trinidad, in the Middle East, in the lower 48, in Canada ... and the list could go on.

The gas market is also shaped by demand. U.S. demand for natural gas has grown by just over 1 per cent per year over the past decade, and growth will continue on the basis of convenience, advances in technology and the environmental benefits of gas consumption against coal or oil.

That demand looks set to continue to rise. On the most recent forecasts from the Department of Energy, up to 2010, U.S. natural gas demand is set to grow by just over 2 per cent per year to a new total of close to 77 billion cubic feet per day.

The market is there, but to win a place in that market, Alaska has to compete against the existing and the potential sources of gas supply from all over the world ... and, because gas is in many cases being used as a substitute for oil and coal, gas from here or anywhere else will have to compete with those other fuels.

And that competition is fundamentally about price.

There is no other reality.

So for us, and for any other investor, any project here has to be competitive with any other project we have anywhere in the world.

Worldwide we are investing \$8.8 billion this year on the exploration and development of oil and gas, and the competition for those investment dollars is fierce.

The next point of reality is our current competitive position in Alaska.

First on oil, and then on gas.

In terms of oil, the competitive position has to be improved.

The challenge is reflected in the cost base.

Operating costs per barrel for us here are 20 per cent higher than our worldwide average.

And pipeline and shipping costs per barrel are four times the average.

Why is that ?

There are a number of interlinked reasons.

Inevitably there is an added cost because the resources are being produced a long way from the markets in which they are being consumed. That is nothing new.

What is new is that Alaska is now a mature, and much smaller oil province. The operating systems and infrastructure were designed for much higher volumes of throughput. As production declines, that means that unit costs are higher.

Alaska isn't unique in facing that challenge. We see the same picture in the North Sea and in other mature producing areas.

In all those areas the figures on cost and on comparative returns matter when it comes to the competition for capital.

And that's why we're doing some very difficult things here.

Taking every unnecessary cost out of the system.

Discontinuing frontier exploration, and focusing instead on exploration in and around existing fields, looking for smaller accumulations near existing infrastructure.

Reducing our staff in Anchorage by 20 per cent and our contractor staff by 75 per cent.

Reducing general and administrative costs.

Looking for opportunities to share services wherever we can, with partners, with contractors, and with Alyeska.

And looking for every practical way to reduce costs, without compromising our commitment to safety and the environment.

These are difficult things to do. But they are necessary and inevitable and they will continue.

We continue to invest here on the basis of the potential which exists. This year we'll be investing over half a billion dollars in Alaska, primarily on new tankers, viscous oil and satellite field development and ongoing infill drilling.

We aim to sustain our investment at that level each year over the next few years.

That investment can only be justified because we believe Alaska can and will

be competitive against the other projects in our portfolio. We are confident that it is possible to respond to the reality of maturity.

We're working hard to achieve that level of competitiveness, but of course we can't achieve it on our own.

We need the help of suppliers and contractors ... and of the State. We need help on costs, and most of all help in securing real, enduring fiscal stability ... and a regulatory structure that strikes the right balance between risk and reward - one that allows for investment and development while protecting the environment.

We ask for that help on the basis that everyone involved has an overriding common interest in maintaining Alaska's competitiveness ... because that competitiveness will bring jobs for Alaskans, business opportunities for Alaskan companies, revenues to state and local governments in Alaska and a reliable, long-term competitive energy supply for consumers and industrial users in America.

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That's about the current reality - the reality of mature fields and oil production which is half of what it was in 1988, and still declining.

Then let's look to the future. To the possibility of developing Alaska's natural gas, which cannot be a reality unless it is linked to a healthy oil business over the life of the development. The billions of dollars we've invested in facilities on the North Slope are underpinned by oil production. Many of these facilities will be needed to produce gas as well as oil. Gas can be one of the legs that will help to carry Alaska into the future, but oil will remain the core.

As I've said, to be viable, Alaskan gas has to be able to compete head-on with other potential sources of supply ... including oil.

At the moment it is not competitive.

Capital costs of \$20 billion, operating costs of \$20 billion and financing costs of \$20 billion.

We and others are working hard to reduce the pre-tax capital costs by applying technology such as advanced high-speed welding, using higher-strength steel and more efficient CO2 removal.

That is work in progress, and on that basis we've set a target to reduce pre-tax capital costs by about \$2 billion.

That would make the development viable on a range of reasonable price assumptions. That is on a pre-tax basis.

But that is not enough.

On that basis, the development of Alaskan gas would still not be commercially viable - because of the fiscal issues.

And that is the point where the issue becomes one of public policy.

Because the decision is about the sharing of the economic rent arising from the development.

As things stand, the current distribution destroys the viability of any such development.

But public policy can change that distribution. There is a case for saying that the public interest lies in setting taxes in such a way that all projects with intrinsic economic merit can proceed.

The grounds for doing that are not sentimental - they are about the hard economic reality which says that by removing an obstacle, you can achieve a net economic gain for all. It is about mutual advantage.

After all, the economic benefit of going ahead with a different distribution of the rent must be higher for all concerned - for Alaska, for Canada and for the U.S.; for those employed on the project; for contractors and service companies, as well as the owners of the resources - than if a project never goes ahead.

And there are successful precedents in the U.S. and in Canada:

- production credits which spawned new technology to develop unconventional coalbed methane and gas in the Lower 48;
- enhanced oil recovery incentives to help extract more oil from aging domestic reservoirs;
- And a variety of progressive royalty and supportive financing measures in Canada to open new energy frontiers in eastern Canada, the tar sands and Mackenzie Valley gas.

Such measures could be revived and used again.

So this is not a debate about subsidy. We are not asking for any subsidy. We do not want corporate welfare.

It is not even a debate about risk reduction. We are ready to accept the normal risks if the project makes sense and can compete effectively on a global basis.

It is a debate about public policy - about the distribution of rent, and about the impact of that distribution on the commercial realities.

Energy security will obviously be part of that debate - because of course it would be imprudent to neglect the development of any resources which can be commercially developed when the world's needs are growing, especially if those resources are only being held back by fiscal arrangements which are not appropriate for the circumstances.

That debate has to be resolved by Governments - Federal Governments and the State of Alaska.

I'm sure those responsible will look at the consequences on a broad front. They'll have to consider, for instance, the consequences for all other energy producers, and they'll have to balance the narrow concerns with the broad public interest.

The role of companies is simply to explain the narrow reality - we can't and shouldn't make the decision on public policy, but we can make clear what we believe the specific, particular implications to be.

Of course, there are other enabling steps which are necessary. Appropriate federal legislation to allow the project to proceed. Fiscal stability at the state level here in Alaska.

An efficient regulatory approval process to allow the gas to be transported through Canada ... and relentless attention to costs at every step.

Those are necessary steps - but it is the commercial reality - the distribution of the economic rent, which will decide the project.

I think both in terms of the immediate challenge - which is to sustain the competitiveness of oil development here in Alaska - and the new challenge of developing Alaska's natural gas - reality is the only place from which to start.

That is what we did 33 years ago.

Then we did something which to many people, including many people in BP, seemed impossible - the development of Prudhoe Bay and the construction of an 800-mile pipeline across some of the most difficult terrain in the world.

We did it, and I remember every day of that period vividly, by focusing on reality, by taking each step in turn, by identifying exactly what needed to be done - and then by doing it. It sounds very simple - but it was very effective.

And because what was done was founded on reality, that development was a source of great pride and excitement. It was soundly based - and there is no greater source of confidence than a strong foundation.

That's what we need to do again now.

I hope and believe we can.

Alaska will remain very important to us ... a cornerstone of our worldwide business.

I believe that with the right sense of reality we can build with confidence on the foundations that have already been established. We can renew the pride and excitement, and the sense of confidence in the future.

Thank you very much.