

Alaska Economic Report

*Tracking resource, business, industry
& construction issues since 1974*

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Special resources brief: Energy supply, Southcentral Alaska

Progress on Cook Inlet gas, but with a catch

There's some progress on securing new Cook Inlet natural gas for Southcentral Alaska, where most of the state's population lives. Enstar Natural Gas has negotiated a new contract with HEX Alaska, a small Inlet gas producer, to supply new gas over three years starting in 2026. This will help but it won't completely meet Enstar's needs of about 40 billion cubic feet per year, so imports of liquefied natural gas, or LNG, are still needed. *More importantly: Much of this is gas is yet to be found. HEX is bullish on prospects it will drill, but the supply is not confirmed.* Having the contract in place is important, however, because it means that once new gas is found it can be moved quickly to Enstar. Think of this as an open-ended purchase order.

What's also important: The Alaska Industrial Development and Export Authority, or AIDEA, the state's development finance corporation, has extended a \$50 million Line of Credit to HEX to finance its new drilling. This is important because it gives HEX, a small company, the cash to work with at its Kitchen Lights field. Also, the state Department of Natural Resources has tentatively agreed to modify the state royalty on gas produced at Kitchen Lights to improve the economics of new gas development there. This must be made final, but that is likely. Kitchen Lights is burdened by not only the 12.5% state royalty but also a 12.5% royalty paid to previous owners of the field. This means Kitchen Lights carries a combined 25% royalty that has to be paid before expenses and a return to HEX.

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Republicans in Congress take aim at Alaska Native 8-A contracts

Bills have been introduced in the U.S. Senate and House by Republican lawmakers that would effectively trim the government's "8-A" minority contracting with Alaska Native corporations. The 8-A contracting has been done for years and has brought hundreds of millions of dollars into Alaska. It is now challenged by Sen. Mike Lee, R-Utah, in S. 5366, and Rep. Grothman, (R-Wisconsin) in H.R. 10216, who argue it is racial preference. 8-A is really aimed at helping minorities secure federal contracts. Major government contractors like Boeing, who are competitors, have lobbied to get the program ended for years. We'll have more on this.

Inside: ConocoPhillips starts up its new Nuna oil project; Armstong and Apache are exploring again

Natural gas supply:

HEX set to drill more, but is there enough natural gas?

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All of this sets the stage for HEX to accelerate its work. There are still concerns. The gas may not be there, or as much of it as HEX is hoping for. There may be drilling problems, as happens in Cook Inlet. There are also high (and rising) costs for Cook Inlet work and the timing as to when Hilcorp Energy can make its jack-up rig available for HEX to use. A jack-up rig is needed for work at Kitchen Lights. Hilcorp owns the rig but must also use it for maintenance and development on its own Cook Inlet gas wells. That's also important to Enstar and other regional utilities who rely on Hilcorp's gas production. HEX has shown that there is undeveloped natural gas. The company recently drilled an exploration well into a prospect near Kitchen Lights and found gas. The well is capable of 2.5 million cubic feet per day. Not a huge producer, but everything will help.

Natural gas is important because it heats buildings in Southcentral Alaska. Enstar has no current alternative to supply this energy, while electric utilities like Chugach and Matanuska Electric have access to hydro power, wind and solar and are planning to add more.

The cost of natural gas to consumers and businesses in Southcentral will be rising

Enstar now pays about \$7.80 per thousand cubic feet on its HEX contract. The new HEX contracts, which are still to be approved by the Regulatory Commission of Alaska, are priced at \$13.69 per mcf or \$12.30 with state royalty relief. This is about what imported LNG is likely to cost, Enstar has said. These increases won't be felt right away because there will still be gas supplied from the older, though declining, Cook Inlet fields, so consumers will pay a rolled-in average of higher-priced "new" gas with lower-priced "old" gas. However, the old gas is being supplied under Hilcorp contracts that will be expiring. There will be new contracts. Our bet is that they will have higher prices.

A wild card to watch: Incoming President Trump's proposed tariffs on imports from Canada. If these happen, and if they include Canadian gas exported to the U.S., the tariff will be added to the cost of the LNG if it is from Canada, which is most likely.

Enstar now says it is short 6 billion cubic feet in contracted supply for 2025. That's a good chunk of the utility's annual need. While the declines in Cook Inlet production from older fields are expected to appear in 2027, short-term gas supply problems are cropping up. If current gas producers (mainly Hilcorp and HEX) can't make up the shortfall Enstar will work with the electric utilities, Chugach and MEA, to reduce their gas use. The electric utilities can fall back on alternatives they have, such as diesel-powered generation and purchasing power from Golden Valley Electric Association in Fairbanks, which has coal and oil-fired power, to be delivered over the Alaska Energy Authority's intertie that connects the Interior and Southcentral grid. This won't be cheap, however. Consumers will pay for it.

Energy: Can we avoid another winter gas supply crunch?

The natural gas near-emergency during the intense cold snap late last January was a painful experience for utility managers and a close call for Southcentral Alaska. It was caused by mechanical failure in wells used to extract gas at a regional gas storage facility near Kenai (gas is injected in summer and then extracted in winter). Since then Enstar Natural Gas, the storage facility owner, has made repairs and drilled two new wells, investing \$67 million (the project came in \$5 million under the \$72 million estimate). That should help on the mechanical side, but Enstar now says that the cold snap few weeks ago took out a considerable volume of gas that needs to be replaced in storage. *Hopefully we'll get through January and February without a repeat of last winter. What's really needed is more gas storage capability, which Cook Inlet gas producer Hilcorp Energy is working on along with Chugach Electric, which owns the majority stake in the Beluga gas field.*

ConocoPhillips starts production at its new Nuna oil project ahead of schedule

ConocoPhillips started production at its new Nuna oil project on the North Slope ahead of schedule and under budget, the company said Dec. 19. Nuna will add about 20,000 barrels per day to North Slope production at its peak, which will likely be reached in 2025. Nuna's production module was built in Southcentral Alaska and moved by sea to the North Slope.

Armstrong and Apache are back exploring east of Prudhoe Bay

Armstrong Oil and Gas its partner, Apache, have resume winter exploration east of Prudhoe Bay, where Armstrong sees good prospects for discoveries. Armstrong is an experienced explorer on the slope and Apache is a major independent with deep pockets. Exploration last winter by the two companies was partly successful but was cut short by bad weather.

Judge's decision in North Slope roads case may set a poor precedent

A judge's decision in a contentious dispute over access to privately-owned North Slope roads handed a first-stage win to ConocoPhillips, the owner of the roads. The court invalidated a state permit that granted free use of the roads to Santos Ltd. for its Pikka project. Santos and ConocoPhillips had reached an impasse in negotiating terms for the road use and the state intervened. The state may likely appeal this to the state Supreme Court because if left standing a private road owner could block a competitor's access to nearby state oil and gas leases. The court suggested use of an eminent domain procedure for future disputes, but that gets complicated and would leave the state as owner of the roads. What's needed is some formal policy for situations like this, which may need state legislation. It's a messy decision which, if left standing, could affect other resource industries, like minerals, which depend on access across state lands.

Defense, government and mining

National Defense Authorization Act has military pay, funds for Alaska

The U.S. Senate has passed its version of the National Defense Authorization Act Dec. 18 and the House version is nearing passage in that body. The bill has a 14.5% pay raise for junior enlisted ranks and a 4.5% raise for all military personnel. The Senate bill also raises the Basic Needs Allowance important for families to 200% of the regional poverty level and boosts child care assistance. The House bill has similar provisions. *This is important for military families in Alaska because current benefits fall short of compensating for living costs, making recruitment and retention difficult here.*

Murkowski says she won't be rolled on Trump appointments

Alaska Sen. Lisa Murkowski, now high-ranking in a soon-to-be Republican U.S. Senate majority, says she won't let incoming President Donald Trump bypass the Senate's traditional role in approving cabinet nominations. According to people who were there, Murkowski told a largely business audience at her "Senator's Holiday Lunch" in Anchorage that her job as a senator is to ensure that cabinet nominees are well-vetted by the Senate for their qualifications, experience, ethics and commitment to the U.S. Constitution. She said she fully intends to do her job as a senator.

Mining: New zinc discoveries near Red Dog promising, but it will be a while before mining

There have been press reports that Teck Alaska's zinc discoveries 10 miles north of the existing Red Dog Mine will "extend" that mine. This isn't quite correct. This would be a new mine. The finds are promising, but years of work are needed. The deposits are also on state lands, not lands owned by NANA Regional Corp., as is the case at Red Dog. Therefore, the 50% net profit share with NANA won't apply at the new finds. Mining at the Red Dog ore body will be depleted in 2031. NANA will undoubtedly be involved in the new mines because Teck will want to use the ore mill at Red Dog and other support facilities that are partly owned by NANA. Teck will also want to use NANA's experienced support contractors which now work at Red Dog.

However, there will be a gap of several years between the time mining ends at Red Dog and production begins at a new mine given the time it takes to explore, permit and develop mines in Alaska. That's particularly so with underground mines like what would occur with Teck's new finds. The economics of underground mines are also more complex than of a surface mine like Red Dog, which is relatively simple in its mining. Exploration drilling at the new discoveries is underway. Teck just got approval for an access road needed to move heavy equipment for advanced exploration. *The gap between the halt at Red Dog and production from a new mine will affect the Northwest Arctic Borough, which depends on tax payments from the Red Dog Mine, which will stop when production ends there. Most of those funds go to support schools.*