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Australian Pipeline Trust
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The Australian Pipeline Trust (APA) previously announced a net profit after tax and minorities (before non-recurring items) of \$45.0 million for the full year to 30 June 2004, up 9.6%. In broad terms, what's the overall profit outlook for the current year and what will drive it?

MD Jim McDonald

There are two major influences on our profit for this year. One of them is the continuing decline in revenue under the Gas Transportation Deed signed with AGL covering the Moomba to Sydney Pipeline (MSP) and the other is the positive benefit we derive from our acquisition of the CMS assets.

We're confident that the benefits flowing from the CMS acquisition will outweigh the lower revenues under the Gas Transportation Deed. Without wanting to put a number on it, we're confident of recording an improved profit after tax in the current year.

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Where are the main opportunities to contract unutilized capacity or expand your existing pipelines? What do you have in mind for the unutilised gas storage facility at Mondarra acquired from CMS?

MD Jim McDonald

Other than the Moomba to Sydney system, Queensland still remains our best opportunity for contracting unutilized capacity. However, in Western Australia, we're investigating "fast tracking" the development of gas storage and de-bottlenecking of the Parmelia pipeline. There is an immediate opportunity created by the delay in the sale of the Dampier to Bunbury Natural Gas Pipeline (DBNGP). Western Power has been forced to take some fairly drastic measures to try to meet summer peak loads, including purchasing of liquid fuel to substitute for gas in their gas turbine generators. The Parmelia storage and pipeline system can supply more gas to Perth if we de-bottleneck it. We can also store gas for use in times of peak power demand to assist Western Power. We're working closely with Western Power to implement this plan.

For the same reason, power produced in the Kalgoorlie district can now be exported to the Perth region. This will result in additional sales on the Goldfields pipeline.

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APA has had mixed success in bidding for WA pipeline assets. You successfully acquired the CMS assets but were an under bidder on the DBNGP. Can you summarise the cost of the CMS acquisition, including debt assumed, and the major benefits?

MD Jim McDonald

The enterprise value was \$318.5 million but the net cash payment by us was \$206 million as we also acquired some debt. The acquisition further diversified our asset base, and we gained commercial control of the Goldfields Gas Transmission pipeline (GGT). We already plan to increase the utilisation of the GGT, through additional compression, and there are opportunities to improve the earnings from the Parmelia system which is presently under-utilised.

The transaction will have an immediate positive financial impact on APA, and there is some upside for us as we take commercial control.

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When do you expect to complete the integration? What are the main tasks?

MD Jim McDonald

The integration is basically complete other than moving some of the Parmelia employees across to Agility. The financial and legal integration is all but done.

Before the acquisition we held an effective 39.7% of the GGT. We understand the pipeline, we know the people, and the cost to integrate the business was consequently low.

The integration of the Parmelia system required a little more attention because it consists of a transmission pipeline, a sales and distribution system in Perth, a storage system and a gas plant. Agility is our operator, and will retain the people,

so that will be seamless, but we have more to learn about the commercial management of it.

As I said before, we're also planning a fast-track project for the storage reservoir.

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APA was successful in having the Australian Competition Tribunal set aside the ACCC's valuation methodology used in the access arrangement on the MSP. However, the ACCC lodged an appeal in August 2004. Can you explain the earnings risks for APA if the ACCC is ultimately successful?

MD Jim McDonald

I remind you that the Moomba to Marsden section of the MSP is unregulated, and revenues on that section will not be affected by the outcome of the ACCC appeal.

Regarding the regulated section of the MSP, in the short term a successful appeal for ACCC will have little impact because of the Gas Transportation Deed. It's important to note that we're considering a different tariff model for what we're now calling the NSW ACT Gas Transmission Grid, which is all our pipelines in NSW except the Moomba to Marsden section of the MSP. It may be quite a different tariff structure than the conventional volume/distance tariff of the MSP system.

In the longer term, all haulage on this grid will be subject to a regulated tariff, but I believe that the earnings risk to APA for our NSW business is low.

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A major objective of APA has been to diversify its portfolio through acquisitions of gas pipelines to reduce the dominance of the MSP in the overall revenue mix. To what extent is MSP's revenue under threat from third party competition and falling gas reserves at the Cooper Basin?

MD Jim McDonald

We're still maintaining our anticipated haulage volumes in the MSP. We're beginning to see third party contracts for gas transported on the MSP in addition to those covered by the Gas Transportation Deed. That indicates that the gas market in NSW and the ACT is freeing up. Additionally, the presence of the SEAGas pipeline into Adelaide suggests that there will be less contract pressure on the remaining Moomba reserves by 2006. Similarly, there is also now less contract pressure on the gas reserves in South West Queensland than there was six months ago, mainly due to the development of Coal Bed Methane (CBM) reserves in Queensland's Surat Basin.

So although we expect the Gas Transportation Deed revenues to diminish over the next year and then bottom out, AGL has already contracted additional capacity beyond 2006 and we also expect others to contract. The tail of Cooper Basin reserves and revenues will be longer and stronger than we suspected it might have been two or three years ago.

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Has the gas industry moved any closer to securing a long term supply of gas for south east Australia? How do you see events unfolding?

MD Jim McDonald

The announcement by Oil Search and their partners that they are moving to FEED (Front End Engineering and Design) for the PNG project is a very significant development. We understand that the scope of the project has changed dramatically compared to that which we understood two years ago, and that there has been a significant reduction in the scope of work and the estimated capital cost of The Highlands Gas Project. I also understand that Oil Search's confidence in the project has grown, and is now shared by Exxon Mobil. That in turn has strengthened our conviction that this project can get off the ground.

I understand that AGL and Petronas have re-mobilized a pipeline development team: that is another positive development for the PNG project.

The task of aggregating sufficient load to get the project away is still formidable, but there seems to be a new confidence that can be achieved. The step change in load necessary for the new supply will be assisted by recent announcements by Origin and the NSW and Queensland Governments that base-load, gas-fired power stations are planned.

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You identified Stress Corrosion Cracking (SCC) on the MSP in a remote area of South Australia and established a pressure management regime. What is the extent of the SCC across the pipeline? Do you expect it to have an adverse impact on operating results and can you give an indication of the capital involved to replace the corroded sections?

MD Jim McDonald

The area of concern for SCC is limited to a hostile soil exposure which exists in the South Australian section of the pipeline. We're running two intelligent pigs through the MSP in the next year. One is a SCC detection pig for that section, and the other is a conventional metal-loss pig which runs the full length of the pipeline. They will cost several millions of dollars but we expect to capitalise most of the costs.

Until such time as we get data from the SCC pig, we can't predict the extent of the cracking. At this stage, we aren't anticipating the replacement of sections of the MSP. The cracks can be repaired by applying re-enforcing sleeves. The cost of any such repairs will impact the operating costs.

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APA is evaluating further diversification opportunities into non-gas transmission pipelines and other investment opportunities. Can you explain what these investments might be and possible timing?

MD Jim McDonald

We're presently discussing installing gas treatment and compression facilities at CBM fields in Queensland. I've spoken about our plans to utilise and expand the Mondarra gas storage in Western Australia, we're considering gas-fired power generation opportunities and we're also now looking at opportunities that are beginning to emerge in water transmission. I don't want to talk about timing yet.

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Looking back over the last year or so, are you satisfied with regulatory rulings and the changes in regulatory environment proposed for gas transmission pipelines?

MD Jim McDonald

I'm satisfied with regulatory rulings because on balance the gas transmission industry won several major appeals and set several significant precedents in regulatory interpretation. It's pretty clear that the Competition Tribunal supports a less forensic interpretation of the Code than the ACCC practices.

The Productivity Commission also completed its inquiry into the application of the Code to gas transmission, and have made some favourable recommendations for change.

However, we await implementation. Our fear is that the Commission's work will be watered down significantly, or lost in political dealing, and that the industry will have to fight for full implementation of favourable recommendations. We also fear that the regulatory regime for the electricity industry will be fixed first and those principles will simply be imposed on the gas industry. We've argued strongly the differences between the management of the electricity and gas industries, but I am not sure the bureaucrats have listened.

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How does APA benefit from gas swap contracts such as the recent one signed between Santos and Origin? What scope is there for more of these agreements?

MD Jim McDonald

The first and obvious benefit for APA is that the swap effectively delivers Queensland gas into NSW. We benefit by increased volumes through our MSP. Secondly, the fact that it is Surat Basin gas also frees up South West Queensland gas for sale into the southern markets or to Mt Isa.

Gas swaps can also work against gas transmission companies because swaps can result in gas being contractually delivered without requiring transmission haulage. Having said that, gas transmission pipelines have effectively interconnected the whole of Eastern Australia so that swaps are possible between any sources of gas supply and we expect these swap arrangements to become more common.

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Can you explain your comment at the AGM that industry rationalisation has now entered a new phase which APA is calling consolidation of the transmission industry?

MD Jim McDonald

The foreign investors in gas transmission pipelines have departed Australia and the industry rationalisation phase is essentially complete. We now see industry consolidation as potentially the next phase for the pipeline and similar industries. We believe we will see some vertical and horizontal integration in the future and that is consistent with our strategy.

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At the AGM you sought and gained approval from the unitholders to facilitate a stapled unit. What's the rationale for that?

MD Jim McDonald

The unitholders have approved the potential creation of a stapled unit if the appropriate circumstances arise to use that form of structure. That's given us additional flexibility and that's really all it amounts to at this stage.

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Thank you Jim.

For further information on Australian Pipeline Trust please visit www.pipelinetrust.com.au or call Jim McDonald on (02) 9693 0011.

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