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Marcellus Midstream 2011: Caiman Energy's Multifaceted Plan

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Driving midstream infrastructure buildout in the Marcellus shale is the need for infrastructure and take-away capacity to handle natural gas liquids (NGLs) from its large rich-gas production area. Speaking at the Marcellus Midstream 2011 conference held recently in Pittsburgh, Jack Lafield, president and chief executive of **Caiman Energy**, detailed the new, but fast-growing company's plans and the role it wants to take in easing the infrastructure crunch.

He noted that the rich-gas acreage in the Marcellus involves an area of 3,000 to 5,000 square miles—to put it into perspective, about the size of the Barnett shale play's core. Echoing the sentiment expressed by a number of presenters at the two-day conference, he pegged the total investment needed to maximize producer netbacks from NGLs and reach markets at "billions."

What's lacking? Sufficient processing and fractionation, an NGL pipeline and a local industrial market. Still, while midstream companies are in the early days of solving these issues, the rates of return are present for both upstream and midstream companies, particularly from the gas-rich areas, to justify the expansions.

These hefty returns are possible even at low natural gas prices. Lafield noted that Range Resources looks for a 74% internal rate of return from its Marcellus production at \$4 on the Nymex, while **EQT Corp.** looks for an after-tax IRR of 78% for its lean gas at \$5. And he pegged the lean-gas netback to producers at \$3.75 per thousand cubic feet (Mcf), vs. \$7.10 per Mcf for rich gas, taking into account residue, processed liquids and condensate.

A significant problem is lack of fractionation capacity in the Marcellus shale region, and Caiman and others are busy constructing facilities to respond. While there is little local market at present for ethane, there is a strong seasonal market for both propane and pentanes-plus, and a marginal regional market for butanes. For example, before the Marcellus shale play kicked off, the region furnished about 15% of the Northeast's supply of propane; since development shifted into high gear, that percentage has soared to 37%.

Lafield pointed out that the rich-gas area is wide, and also has a wide range of ethane, from 8% to 16% in some cases. Currently, options involve blending ethane with leaner gas and traditional gas coming up on the Tetco line; its specifications permit 12% ethane. "Lean gas upstream and downstream allows producers to flow significant quantities of rich gas into Tetco," Lafield said. "This buys time to review options to enhance value."

Other alternatives are the Sarnia, Ontario petrochemical market, via Nova/Imperial pipelines, or the Gulf Coast petrochemical market via pipeline or ship. Newbuilds and reactivation of local facilities may provide the ultimate solution.

Meanwhile, ethane supply is nearing the point at which it is expected to top demand. This could have an impact on pricing, as lower frac spreads would make it difficult to justify expensive ethane solutions, even in times of under-supply, Lafield noted.

Caiman was founded in 2009, but its executives bring to the table more than 100 years of industry experience. The company refers to itself as "everything midstream," and the steps it is taking to add capacity in the Marcellus reflect this approach with an investment of more than \$200 million in capital to date. It has completed Phase 1 of the Fort Beeler cryogenic plant, which provides 120 million cubic feet per day of capacity. (In July 2010, Caiman secured \$380 million in equity commitments.) Some 50 miles of 6- to 24-inch planned gas-gathering lines are finished. It has six operating compressor stations, and has constructed 35 miles of condensate pipeline.

In January of this year, it signed a gas-processing agreement with **Chesapeake Energy Corp.** and **Statoil**. And it has formed a marketing alliance with Inergy to take customers NGLs to wholesale and retail markets, and has an agreement with Tetco for residue gas.

Phase 2 of the Fort Beeler plant in Marshall County will add 200 million cubic feet per day of capacity by January 2012, and a third phase, also scheduled for completion in 2012, would add another 200 million.

Another 80 miles of gathering lines are under construction. Further, it plans to build NGL facilities on the Ohio River, including a Y-grade line by this July, and a fractionation plant and terminal are under development with a Phase 1 ability to take 12,500 barrels per day by year-end 2011, and another 15,000 barrels per day in 2012. All told, it anticipates investing up to \$400 million in 2011.

With all this infrastructure development under way, however, Lafield suggested there is ample room for more. The Marcellus shale's size, significant amount of rich-gas acreage and close proximity to gas markets means there's still a big piece of the puzzle missing—a total solution for reaching those wonderful markets.