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Portfolios in The Balance

One of the important risks we face is not a technical risk but a growth risk. The risk that with highly volatile commodity prices the portfolio won't increase value.

This risk can be mitigated by balancing the portfolio with projects of different characteristics. One of the characteristics, little discussed but of extreme importance, is the production profiles. These control cash flow, hence the money.

Consider the end points of production spectrum - high decline (e.g. fractured reservoirs) and flat decline (e.g. coalbed methane). Each has a high risk of failing to meet the growth targets. The high decline wells stress the system because a high number of wells are required to keep production flat. Reinvestment risks, large inventories, and price volatility make sustained growth difficult.

The long delay until positive cash flow in a coalbed methane project makes its ROR miniscule and significant growth almost impossible. Once running it can not be shut down to adjust to the vagaries of price.

Combining these types of projects, we can develop a portfolio, which has sustainable growth of 5 - 10% with minimal risk. Such portfolio can react to price changes and investments can be shifted.

While our portfolios are more complex than this two-project example, they are similar. Mitigating our risk by balancing the portfolio with projects of differing production profiles will allow us to successfully manage our companies in both the short and the long run.