

OMV Petrom Q4 2019 Conference Call – Q&A Transcript

OMV Petrom published its results for Q4 and January – December 2019 on February 6, 2020. The investor and analyst conference call was broadcast as a live audio-webcast at 3:00 pm local time. Below is the transcript of the question and answer session, by topic, edited for readability.

Group

1. Proposed legislative changes / Neptun Deep

Question from Tamas Pletser (Erste Bank): Regarding the current political situation and the current regulatory changes in Romania. In light of the recent government move, that there is no government in Romania, how does it affect, in your view, the proposed changes in the regulatory environment, especially the Offshore Law?

Answer from Christina Verchere (CEO): I will share some views on the political situation or maybe how does it affect the energy sector.

Firstly, I think – which I mentioned in the presentation, the restoring of investor confidence in Romania, particularly in the energy sector, took one-step forward with the passing of GEO 1/2020 and an accelerated move back to a liberalized gas market. I think this is a very important move that actually we talked about at the end of last year.

The second thing that we have heard is a desire to create changes to the Offshore Law and the one thing we have heard the minister of economy talk about, is the desire to have multi-party support and political consensus for this. It is our understanding that this will be put into parliament and therefore will be a parliamentary process. Right now we have an interim government because of the vote that happened yesterday, but if it is a parliamentary process that should not affect this. If I asked you to look out for one milestone, which is the milestone that we are looking for, is when an Offshore Law is put into the parliament.

Question from Tamas Pletser: I remember you said I think last time that potentially you can still make the FID on Neptun during the second half of the year. In light of the current changes as to when the Offshore Law can be approved, do you still see the chance that this FID can be made in the second half of the year?

Answer from Christina Verchere: I think you might find you have not heard me say anything about the timing of FID. But I think what I would say is once the Offshore Law is passed, after that we will be then looking to understand and confirm the costs of the development concept, look at the project economics and then go through internal governance.

The FID decision requires agreement between the titleholders. So, if you pushed me hard on it, I would say once we see the Offshore Law, and we have to see the Offshore Law passed, perhaps you could see between nine to twelve months. But we really need to see the Offshore Law passed and know what is in it because it is going to tell us about the sort of economics of the project as well as the stability. We are looking hard at the stability clause and the competitive terms that we think are needed to allow this project to move forward.

And then if I had just one other comment with regards to timing, we say first gas for a project of this size and complexity– we have said and we will say it again, we estimate about four years from FID to first gas.

Question from Oleg Galbur (Raiffeisen Centrobank): There were some rumors that Petrom might be interested in increasing its stakes – its participation in the project, and I was wondering what is your view on that. Are you happy with this percent? Or you would consider it depending on some terms?

Answer from Christina Verchere: We have a company policy that we do not comment on any M&A activities or any rumors that are going on in the market, so I am supposed to honor that company policy. But what I would just reiterate is what is most important to us right now, is to get what we have to work. So, the big milestone we are looking for is the Offshore Law. With the Offshore Law, it can see if it can unlock what I think is a huge opportunity, obviously for OVM Petrom, but is significantly actually for Romania as well.

Upstream

1. Production decline

Question from Tamas Pletser: You mentioned in the presentation that you expect in 2020, a below 5% decline in oil and gas production. How does it split between oil and gas? Is it going parallel or is it going more gas or more oil?

Answer from Peter Zeilinger (EB member Upstream): The decline is as we have seen last year, we had 2% decline in oil and ran at about 7% decline in gas and we also expect a higher decline in gas for this year, simply due to the fact that the main gas-producing fields that were on plateau until 2017 have entered the decline phase and are continuing to go down. Now, we might look at this in the middle of the year again, but this depends on the drilling result that we have and the testing, but so far, with what we know from the existing portfolio, this is rather higher in gas and less in oil.

2. Sale of marginal fields

Question from Oleg Galbur: The follow-up on the production outlook for this year. You are planning to divest some 40 marginal fields, by half of this year and I was wondering what is the cumulative output of those fields, and maybe you have a split by oil and gas.

Answer from Peter Zeilinger: With the pace that we have seen in the past, we do not expect that there is a closing in the first quarter, rather see end of the second quarter, but it depends completely on the pace of the regulator. Currently, those fields are producing roughly 1,700 boe/day. In the past, what we divested was 80-20, more in oil. These fields are representing roughly 1% of our current production level. On the oil-gas split, I just checked my notes. It is heavier on gas. So, 60/40 more gas than oil for the 40 fields. So, not that significant and I expect a closing not before the middle of the year.

Downstream Gas

1. Gas market prices

Question from Iuliana Ciopraga (Danske Capital): Could you share your views of gas prices. There is still a large gap between Romanian gas prices and European hub prices. How do you see that gap developing in 2020?

Answer from Franck Neel (EB member Downstream Gas): Concerning the gas price, I think if we look at why there was a gap in 2019, if we compare CEGH and Romanian gas prices, first, we have to be careful when we compare a platform hub. I mean, the liquidity of the Romanian hub is very small. And we have to keep in mind that a lot of transactions, especially to the regulated markets, was done outside of this platform.

But the main reason was that we have the decline of production; we had an increase of storage obligation which was significant and also a market player was concerned about the risk in Romania. Romania was really at risk if there was an interruption from gas supply from Russia to Ukraine and compared to other countries we are quite at risk. So, some players also increased the storage for this reason. And the lack of interconnection between the closest market, the CEGH, the Austrian market and Romania. That explains mainly the gap you have seen in terms of gas price. If we look at 2020, you are right. We see more reduction of this gap potentially in 2020 because, first of all, interconnection has improved, so we see a better interconnection between Romania and the closest market. Winter has been very mild, so we have quite a lot of gas still in storage, which will influence certainly summer prices. We do not expect also an increase in demand. So, we see a reduction of the gap for this business.

And again, just to clarify, we still see a premium on the Romanian gas price versus CEGH for 2020.

2. 2% financial contribution to ANRE

Oleg Chistyukhin (Renaissance Capital): Could you please just verify if this 2% tax on gas turnover that we witnessed in a couple of past quarters has been eliminated beginning January of this year?

Answer from Alina Popa (CFO): We had introduced this 2% tax on turnover starting beginning of 2019 based on the GEO 114. This was covering both gas and power. Concerning the impact of such tax, it was for the full year 2019, a P&L impact of approximately 92 million RON. This tax was recently abolished by the ordinance 1 in 2020, so we do not expect to pay a similar amount for this. It is replaced for power by 0.1% of the turnover on the licensed activities and with an amount 0.168 RON per MWh in case of gas.

Downstream Oil

1. Marine fuel oil production start

Question from Oleg Galbur: My first question is on the marine fuel oil that you mentioned that you start producing. I was wondering if you could share with us how is the demand for this type of fuel developing as well as how are the crack spreads comparing to diesel for example. Do we see high potential going forward? Or you are rather disappointed at least since the beginning of the year, as the diesel and heavy fuel margins have been developing in different directions than everybody had expected?

Answer from Radu Caprau (EB member Downstream Oil): We said that we are in a good position to capitalize on IMO opportunities but on top of it, we have developed this product with a maximum 0.5% sulfur content that we have put into the market, in Constanta market. Difficult to estimate now how the market will move and how it will react in the future considering the uncertainty around it. We have delivered the first volumes, so we are present in Constanta.

While talking about cracks, I think it is fair to say that marine fuel oil has started 2020 on a relatively strong note. While for the diesel cracks, they remain subdued, due to a mild winter in Europe and HSFO quotations decreased towards the end of Q4. However, the fuel oil cracks seem to be a bit stronger than expected due to the opportunities for transatlantic arbitrage.

Question from Oleg Galbur: I have just one short follow-up on my question on marine fuel. What is your current production capacity? Or what is the yield that you can achieve in this product?

Answer from Radu Caprau: For that one, to be able to have the product, we have made a minimum investment of approximately EUR 3 million, but it is a matter of optimization to be honest and it is difficult to give a sharp number on how much we could go ahead on that. The fact is that we want to have a say in Constanta, and as said, we are optimistic about the opportunities there.

2. Downstream Oil capex

Question from Iuliana Ciopraga: First regarding CapEx. So, you expect CapEx of around 4.2 billion in 2020, out of which about 2.3 billion in Upstream. Could you give us some details on the remaining part? Where will that be going?

Answer from Radu Caprau: Most of our investments are going in refining and in retail. When we talk about refining, we refer especially to the bio-compliance. We need to finalize our investments in order to ensure a full bio-compliance for this year, and we are preparing ourselves for a long-term compliance as well from a bio perspective by looking at our core processing in Petrobrazi.

If we talk about retail, we would continue our investment in ensuring that we are having a solid presence into the market and we continue our profit improvement projects, as said.

Question from Iuliana Ciopraga: Regarding the investment in Downstream, is this level of investment in Downstream expected to continue? Should we expect this level of investment going forward as well?

Answer from Radu Caprau: The approximate level is a relatively constant one for Downstream Oil investment, but of course we need to look as well on what is going to come from the projects that we are having right now in the pipeline; we are still looking at opportunities to see what are the projects that we could potentially develop in Brazi from petchem perspective. So, once we are having a review on the choices, then investments could potentially go higher.

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