4Q19 Earnings Conference Call
Edited Transcript

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This transcript has been edited by Chevron Corporation. It is generally consistent with the original conference call transcript. For a replay of the Investor Conference Call, please listen to the webcast presentation posted on chevron.com under the headings "Investors," "Events & Presentations."

Transcript

Operator:

Good morning. My name is Jonathan, and I will be your conference facilitator today.

Welcome to Chevron's Fourth Quarter 2019 Earnings Conference Call. As a reminder, this conference call is being recorded. I will now turn the conference call over to the General Manager of Investor Relations of Chevron Corporation, Mr. Wayne Borduin. Please go ahead.

Wayne Borduin (GM Investor Relations, Chevron Corporation):
Thank you, Jonathan.

Welcome to Chevron's fourth quarter earnings conference call and webcast. Our Chairman and CEO, Mike Wirth, and CFO, Pierre Breber, are on the call with me. We'll refer to the slides that are available on Chevron's website.

Before we get started, please be reminded that this presentation contains estimates, projections, and other forward-looking statements. Please review the cautionary statement on Slide 2.

Now, I'll turn it over to Mike

Mike Wirth (Chairman and Chief Executive Officer, Chevron Corporation):
Thanks Wayne.

Last March, I laid out Chevron's strategy to win in any environment – focused on four elements that differentiate Chevron from its competitors - an advantaged portfolio, a resilience to price downside, a commitment to capital discipline, and a superior capacity to return cash to shareholders.

And as we've done in the past …we delivered again in 2019. We generated over $27 billion in cash flow from operations. We executed our $20 billion capital program. We grew annual production to a record high. We continued to high-grade our portfolio, and we further strengthened our industry-leading balance sheet.

As result, earlier this week we increased the dividend by more than 8%. And we expect to sustain the increased share buyback rate of $5 billion per year going forward. And we did this despite the cost increase at TCO and the fourth quarter impairments – which Pierre will cover in a minute.

Our 2019 performance delivered on all four of our financial priorities – which I'll cover on the next slide. These financial priorities don't change. They've been the same for a long time.

For two years in a row, we simultaneously increased our dividend … increased share repurchases … grew production … and reduced debt. Not everyone can say this. You can see the sources and uses of cash on the slide, including the $13 billion returned to shareholders, nearly the same amount as our cash capex.

2019 was a good year, and we intend to do even better. During our Analyst Day in March, we'll lay out our plans to further improve performance in order to continue to deliver superior returns to shareholders.

With that … I'll turn the call over to Pierre who'll discuss our 2019 financial results.

Pierre Breber (Vice President and Chief Financial Officer, Chevron Corporation):

Thanks, Mike. Turning to slide 5.

Fourth quarter's results included a net $9.2 billion charge in special items and a foreign exchange loss of $256 million. Excluding special items and FX, earnings were $2.8 billion, or $1.49 per share. A reconciliation of non-GAAP measures can be found in the appendix to this presentation.

Cash flow from operations was $5.7 billion… this is lower than the prior quarter in part due to higher taxes on repatriated cash, including the cash impact for the $430 MM tax charge that was accrued in the 3rd quarter.

Total capital spending was $21 billion. This includes around $800 million of inorganic spend, which we don't budget, primarily relating to the purchase of the Pasadena refinery and acquisition costs for exploration leases and additional working interest in El Trapial.

Return on capital employed was about 7% when adjusted for special items and FX. We're committed to improving returns on capital … and we'll share more about our plans to do so at our Analyst Day in March.

Importantly, our strong free cash flow enabled us to pay over $2 billion in dividends and repurchase an additional $1.25 billion in shares in the quarter. As Mike mentioned earlier, for the full year, we returned $13 billion in dividends and share buybacks to our shareholders.

And we end the year with a stronger balance sheet – and the lowest debt ratio among our peers. Turning to slide 6.

In the 4th quarter, we recorded over $10 billion in impairments and write-offs. These were triggered in December by our decision to reduce funding to various gas-related opportunities and to lower our long-term oil and gas price outlook. Line item detail is available in the appendix.

While we're disappointed by these charges, we're confident that we're making the right decisions to prioritize our capital on our most advantaged, highest return assets.

These charges were partially offset by a $1.2 billion gain from our UK asset sale.

Turning to Slide 7, excluding the impact of special items and FX, earnings decreased $3.6 billion in 2019 compared to the prior year.

Upstream earnings declined primarily due to lower commodity prices partially offset by higher liftings. Downstream earnings also were down due to lower refining and chemical margins together with lower volumes – due primarily to the Southern Africa divestment.

The "Other" segment charge, adjusted for special items and FX, was modestly higher, but in line with full year guidance of $2.4 billion. On slide 8…2019 production was a record 3.06 million barrels per day, an increase of over 100 thousand barrels a day… or more than 4 percent from 2018. Excluding the impact of 2019 asset sales, production grew by 5.4 percent, right in the middle of our 4 to 7 percent guidance range.

Shale and tight production, primarily in the Permian, and the ramp-up of Wheatstone and other major capital projects, increased production by 235 thousand barrels per day. This growth was partially offset by base decline and the impact of asset sales, primarily in Denmark and the UK.

Turning to Slide 9 and our reserves replacement. In 2019, our 1-year reserve replacement ratio was 44% … our decision to reduce capital funding to Appalachia natural gas resulted in a negative revision of about 400 MM BOE of proved undeveloped reserves – and asset sales reduced reserves by another 100 MM BOE. Adjusting for these two items, reserve replacement was around 90%.

Annual reserve replacements are lumpy by their nature. Five-year reserve replacement ratios are more meaningful and ours is 106% … highlighting our continued focus and sustained ability to replace the proved reserves that we produce over the longer term.

Slide 10 highlights some recent commercial developments. First, we acquired an additional 15% working interest in the El Trapial field in Argentina – giving us 100% ownership of the conventional production and the unconventional potential in this block.

We also recently announced an agreement to acquire terminals and retail sites in Australia – allowing us to further integrate our refinery production in Asia with a strong retail network after the deal closes.   Late last year, we also signed agreements to sell our interest in our upstream assets in Azerbaijan and Colombia. Both transactions are expected to close in the first half of this year.

And a few weeks ago, we joined the Hydrogen Council, building on our knowledge and experience with hydrogen and our commitment to explore ever cleaner energy solutions for the future.

With that, I will turn it back to Mike.

Mike Wirth:

Thanks Pierre.

On slide 11, we're maintaining our commitment to capital discipline – and in 2020 our capital budget will be flat for the third consecutive year. The stacked bar depicts our organic C&E budget of $20 billion, which includes more than $6 billion in expenditures by affiliates, primarily TCO, CPChem, and GS Caltex.   In the 2020 budget, approximately $5 billion is allocated to our upstream base business, $4 billion to FGP / WPMP, another $4 billion to Permian development, $3 billion for downstream and chemicals, and the remainder goes to other MCPs, exploration, and other projects.

Chevron's capital program is unlike our peers. Our spend profile has low execution risk and is focused primarily on short-cycle, high-return investments that are expected to sustain and grow the enterprise for many years to come.

Slide 12 shows our production outlook for this year, assuming a $60 Brent price. We expect production to be up to 3% higher than last year, excluding the impact of any 2020 asset sales.

Our projected growth is largely driven by the Permian …. partially offset by ordinary base declines and the effects of prior year asset sales. The 3% range reflects key areas of uncertainty in our business as noted on the slide.

After another record year of production in 2019, we expect a fourth consecutive year of production growth, excluding the impact of potential 2020 asset sales.

Moving to slide 13, I'll share a few closing thoughts. As I've mentioned before, we intend to win in any environment. We're not making excuses for tough commodity prices or margins. As a result of our advantaged portfolio, capital discipline, low execution risk, and financial strength --- we're well positioned for 2020 and committed to maintain organic capital spending at $20 billion and return significant cash to shareholders through our dividend and buybacks.

More detailed guidance related to the first quarter and full year is in the appendix. With that, I'll turn it over to Wayne.

Wayne Borduin:

Thanks Mike.

I'd like to remind everyone that we have our annual Security Analyst Meeting in New York in early March, where we will share more about our business performance, long-term strategies and 5-year outlook. We're looking forward to seeing you there. For those not attending in person, it will also be available via live webcast.

That concludes our prepared remarks. We're now ready to take your questions. Keep in mind that we do have a full queue, so please try to limit yourself to one question and one follow up, if necessary. We'll do our best to get all of your questions answered. Jonathan, please open the lines.

Q&A

Operator: Our first question comes from the line of Neil Mehta from Goldman Sachs.

Neil Mehta (Goldman Sachs):
For the first question, Pierre, the earnings look good in the quarter, cash flow looks a little light... It did seem like there were some one-time items in there. So, can you spend some time talking about what some of those one-time items are and how should we think about that rolling off as we go into the next quarter?

Pierre Breber:
Yes. Thanks, Neil. Cash flow was a little light. In the third quarter, we did provide guidance that we expected to pay the taxes on the repatriated cash. If you recall, in the third quarter, we accrued in our P&L for that tax effect on repatriating cash, but the cash taxes weren't actually paid until the fourth quarter, when in fact you saw the cash move. So, you saw cash balances go down from over $10 billion to less than $6 billion at year-end.
The second item I would add was lower affiliate dividends. We had lower dividends from our chemicals affiliates, Chevron Phillips Chemical Company, and no TCO dividend in 2019. At times in years past, we received a dividend from TCO in the fourth quarter, and we didn't have that last year.

Neil Mehta:
Great. And the follow-up is on production guidance, up to 3% and there are a number of variables that you called out there. But can you talk a little bit more about how you think about volumes in 2020? What are some of the pluses and minuses that we should be focused on? And how should we think about some of the timing of those elements, recognizing that you're solving for value over volume?

Mike Wirth:
Yes. Neil, I'll take that one. We've had, as I mentioned, 3 years of production growth, 7% 2 years ago; 4.5% last year; 5.5% without asset sales. We continue to be on a good, strong program in our upstream that's delivering volume growth and, as we said, up to 3% this year. The Permian is the biggest piece of that. And you can see over the course of 2019,

we delivered. And we're at, what I would call, full factory production mode right now in the Permian. That machine continues to click along very well. Jay will talk more about that, including not only the near-term view, but lay out a little bit of a longer-term view for you in March.

We've got contributions from other shale and tight, where we continue to invest in both Canada and Argentina, and those are beginning to contribute - not at the same magnitude as the Permian, but, certainly, strong growth. Gorgon and Wheatstone, through improved reliability and addressing constraints and optimization within the LNG plants. So, we've got growth coming across a number of those [assets].

And as you note there, we've got some uncertainties on the PZ. It looks as if we will begin production there at some point over the next few months. There's still some details being worked out, but that starts to come back in. Hard to say how things go in Venezuela - really difficult to say right now.

And then the other one, of course, is non-operated joint ventures. And we certainly have some expectations for activity there. How that trends with funding levels, decisions by partners, et cetera, is a little hard to predict. But we expect to grow production again this year, as I said, setting aside if we do anything else with asset sales in the portfolio.

Fundamentally, the underlying drivers that we laid out last March - where we set a 3% to 4% compound annual growth rate over the next 5 years - those drivers remain intact.

Operator: Our next question comes from the line of Phil Gresh from JPMorgan.

Phil Gresh (JPMorgan):
The first question here. Some of your peers seem to be signaling a retrenchment on buybacks, to protect balance sheets. Obviously, you've talked about the strength of your balance sheet and a willingness to continue the $5 billion buyback here in 2020, despite the big increase in the dividend earlier this week. So, as you look at that, is there any reasonable scenario where you would think it would not make sense to do the buyback from a macro perspective? I know a year ago when you put this in place, the idea was it would stay there through most reasonable cycles. So just your latest thoughts on that.

Mike Wirth:
No change in our expectations there. We increased the buyback last year. If you look at our cash flow, you can see that we certainly can afford this. As Pierre mentioned, debt came down again last year, and we have the capacity to see this through cycles, which is what our intent is. And no change to that guidance at all.

Pierre Breber:
If I can just build off that and address Neil's question on fourth quarter cash flow. If you look at full year cash flow, it was very strong. Again, we paid a higher 6% dividend per share in 2019. We fully funded our capital program and grew production, as Mike said, over 4%. We paid down more than $7 billion of debt. And in 2019, we bought back $4 billion of shares. So, we're exiting the year confident on our ability to generate future cash. That was expressed with the 8.4% dividend increase and, again, this expectation of sustaining the buyback through the cycle.

Phil Gresh:
Okay. Great. Mike, second question. Just a follow-up - it sounds like you've been doubling down here on cost reduction efforts, and it's been a big focus for you recently. So, it would be helpful if you could talk about what's been happening lately on that front. Do you see this as something that would be material to investors in terms of Chevron's ability to reduce cost in the upstream and/or downstream businesses in the way that we could see?

Mike Wirth:
Yes, Phil. So, I may sound like a broken record on this, but in a capital-intensive business, capital discipline always matters. And in a commodity business, cost discipline always matters. We've done a good job in taking costs out of our business over the last several years in response to the downturn we saw earlier last decade. You can never assume that you're done when it comes to seeking efficiency and driving to an even more efficient cost structure. So, my expectation is we're going to continue to look for ways to do that. We've taken costs down at the same time as production has grown significantly over the last number of years, so unit costs have come down dramatically. And my expectation is we're going to continue to look for ways to reduce both absolute costs and unit costs over time. In March, we'll lay out a little more specifically what some of our ambitions are, and these are the kinds of things you can expect to see.

Operator: Our next question comes from the line of Jason Gammel from Jefferies.

Jason Gammel (Jefferies):
Another solid year in terms of execution in the Permian. I was hoping that you could address whether you still see the Permian as on target, being able to be essentially free cash flow positive. The capital budget ticked up a small amount for 2020, and I know commodity prices have some influence there. But if you could just talk about what you're seeing.

Mike Wirth:
The short answer to that is yes, we do. We fully expect to be cash flow positive in the Permian this year. We exited the fourth quarter with very strong production if you look at the growth Q3 to Q4. And across all the metrics, we continue to see improved performance. We're getting more feet drilled per rig every year, lateral lengths are increasing, EURs continue to go up, development costs continue to come down. And we are becoming more efficient from both the capital and an operating cost standpoint. You put all that together with the royalty barrels and the benefit of the fee acreage that we hold, and the picture in the Permian looks as strong as it ever has. It just gets better.

Jason Gammel:
Great. And then just as a follow-up, and this may be something that you prefer to largely defer to March. But a lot of your European peers are putting a fairly significant amount of capital into businesses that they call “low-carbon”, which generally look to be relatively low rate of return type of investments. Can you talk about within Chevron how you think about lowering the overall carbon footprint of your portfolio and whether these are the types of investments that make sense for you?

Mike Wirth:
So, let me start with lowering our carbon footprint, and then I'll come to investments, Jason. We absolutely are committed to lowering the carbon intensity of our operations. Last year, we announced two metrics tied to methane emissions and flaring that are driving significant changes in what we do. We have adopted two additional metrics, which I expect to also be included in compensation related to carbon intensity of oil production and gas production. We are doing a lot of work around marginal abatement cost curves across our entire portfolio to look at the intersection of technology, investment and opportunity to reduce our carbon footprint.

We're integrating renewables into our business in a much greater way with green power purchase agreements, feeding biofeedstocks in our refineries as soon as this year and co-developing renewable natural gas projects with dairy farmers, for instance.
And then the final thing is we are investing in technologies, looking for things that can scale up, that can provide solutions to these challenges. And this includes not only things like carbon capture from ambient air, but other things to try to decarbonize the more difficult sectors where energy intensity is high. Last thing I'll say is, just to remind you, that

we operate the largest on-purpose carbon capture and storage project on the planet at Gorgon. And we have two of the trains running right now. The third will start up this year. At full capacity, we will be sequestering 3.5 million to 4 million tons per year. So, we're absolutely committed to finding ways to address the climate issue.

When it comes to investments, it can be challenging because the returns, as you say, historically, have not been competitive with some of the other things that we invest in our portfolio. We're looking for ways to improve that and find things that we can invest in that would offer attractive returns for investors, also be good for the environment and, importantly, can scale. And this is a big challenge, and we need things that we can do at scale. We continue to be committed to that.

Operator: Our next question comes from the line of Jeanine Wai from Barclays.

Jeanine Wai (Barclays):
Last month, Mike, you were quoted by saying that companies that wait until change is forced upon them fail. And we were just wondering, are those comments specifically related to the gas write-downs and Chevron's longer-term view on natural gas versus liquids? Or was it more broadly speaking to Chevron's strategy related to the energy transition or something else?

Mike Wirth:
Probably the ‘something else’. We need to continue to adapt. Our company has been around for more than 140 years, and we have reinvented ourselves many times over that period of time. We live in a world today with 7.5 billion people. 20 years from now, there will be more than 9 billion people on the planet. There's an expectation for a reduction in the impact of what we do. And at the same time, we need to support affordable, reliable access to energy for a growing population and growing standard of living. Now we also have technology tools that are available today that we've never seen before. What we need to do is continue to evolve our culture, our applications of technology, our cost structure, our competitiveness and our discipline to be part of that equation for many, many decades into the future. So, my comments really are a message to our employees that we need to change, we need to evolve, and it addresses all of the things that we've talked about. It addresses a more efficient and lower carbon intensity in our operations, but also calls for us to find ways to adopt new technologies and change the way we work in response to them.

Jeanine Wai:
Great. That's very helpful. My second question is on the Gulf of Mexico and potential upside to medium-term growth there, especially post 2023. So, with tiebacks to existing infrastructure, they are very attractive from a rate of return perspective in the portfolio. Can you talk about any technology that you're working on that could potentially extend tieback ranges? And then any update you might have on estimated resource that we can be excited about in terms of exploiting through existing facilities or infrastructure given the continued focus on free cash flow?

Mike Wirth:
Yes. We've sanctioned a project at the end of last year, which is a greenfield project at Anchor - at a much lower cost structure, both capital cost and operating cost, than we've seen before. I think when we find projects where that's the right answer, you'll continue to see us do that. And we've got a lot of exploration acreage out there and a good track record over time on exploration. But the concept of tiebacks, I think, is one that we need to continue to invest more in. We had a discovery last year with Hess as the operator called Esox, a low-cost, high return tieback, which actually will turn a 2019 discovery into 2020 first oil. It's about 5 miles away from Tubular Bells. We've been working on technology to extend subsea tiebacks. This includes longer distance pumping of fluids, compression and movement of liquids, and the ability to avoid formation of hydrates and other things on the sea floor. Pushing the range of tiebacks from the neighborhood of 30 miles out closer to 50 miles really expands the opportunity set for us to use existing infrastructure

to improve production. We're working on multi-phase subsea pumps and a number of these technologies. So I think, as we go forward, what you will see is an increased blend of tiebacks and use of existing infrastructure as well as the occasional large greenfield project that comes in. Things like Anchor, for instance, you've got an initial phase of development. And once that's in, that enables what I just described, which is these additional follow-on phases of development, which are much more economic. I think technology just moves in one direction, and it really builds on my prior comments that we need to look for ways to use technology standardization and other approaches to make the deepwater even more economic. A lot of progress has been made on that, and I'm optimistic we'll see more in the future.

Operator: Our next question comes from the line of Roger Read from Wells Fargo

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Roger Read (Wells Fargo):
I've got one that's maybe on the risk side question and one that's on the upside question. So, with the good news first, you highlighted some of the things that are risks to 2020 production, but recent talk has been about restarting the neutral zone. You have a position there. And then I was curious where else we could see some upside in the portfolio in 2020. Should we be thinking Permian? Or should we focus on some other portion of the operations?

Mike Wirth:
Yes, Roger. So, on the Partitioned Zone after several years of being shut down, there's been progress with an agreement between the Kingdom of Saudi Arabia and Kuwait. That memorandum of understanding has now been ratified by the Royal Court in the Kingdom and the parliament in Kuwait. And we're moving on to some administrative actions required to implement that. All of that suggests that we should resume work in the PZ this year. It's been shut in since May of 2015. And so, we will be careful to ensure that any start-up and resumption of activity is safe, that we really focus on equipment integrity, so it will be a careful restart and a gradual ramp. I think in terms of production this year, we're likely to see a start-up at some point and then some work before we begin a gradual ramp. So, what that nets to is not a lot of impact this year. But it could be some positive upside. I think we'll see more of the ramp completed in 2021. We eventually will have to get some new rigs in there to begin drilling additional wells, but it should be on a trend line over the next 18 months or so back towards something that we saw before we shut down.

In terms of other upside, the Permian has continually surprised us to the upside, even as we raise expectations in the past. So certainly, that is a possibility. I mentioned the other shale and tight, and those also continue to really show strong improvement in terms of performance. So, I think those are some other areas where you could see production upside.

Roger Read:
For my bucket of cold water on you. We've seen global natural gas prices take quite a hit. Obviously, fairly mild winter across Northern Hemisphere hasn't helped. But part of it is your own LNG facilities and everyone else’s continues to run better than expected and some start to run above nameplate capacity. As we think about gas in 2020, do you feel that as we look at North American forward curves, that's probably a pretty good indicator of the year ahead? Or is there a reason for optimism in one place or greater pessimism in another? Just sort of curious how that would fit into your outlook.

Mike Wirth:
Overall, Roger, I think the market is, as you say, pretty tempered on gas pricing. And we have had a relatively mild winter, both in North America and in Asia. And forward markets reflect that inventory levels reflects that. We're not banking on a recovery in gas prices. We're underweight gas as a percentage of our portfolio versus others. And I'll remind you, we've got pretty good term contracting on our LNG with oil-linked pricing across a lot of our portfolio there.

So, from a relative weighting standpoint, we may not be quite as exposed. So maybe it was a bucket of cool water rather than ice water that you dumped on me there. But yes, the markets are setting up, I think, to be pretty flattish. And that's why we've got to focus on self-help and things like cost, as I discussed earlier.

Operator: Our next question comes from the line of Doug Terreson from Evercore ISI.

Doug Terreson (Evercore ISI):
Mike, so integrated oil returns on capital have converged between the companies during the past decade or so, which suggests that competitive advantages may be converging, too. And on this point, while you guys have this mantra of disciplined returns-driven capital allocation, and that's clearly the appropriate approach, at least in my view. My question is whether you think that historical advantages in project management, multinational experience, technological superiority, cost of capital, et cetera are still strong and defendable for Chevron. And if so, are there examples that underscore the strength of the advantages that you guys have? And on the other hand, are there areas of historical competitive advantage that you sense are being eroded and where you'll need to redeploy capital away from in the future?

Mike Wirth:
Well, there's a lot in there, Doug. Number one, you're right. I think we have seen this convergence of returns, in part by the last cycle we came through in high prices. We had a high cost structure. We had a lot of investment across the industry. And we are now living in a world of more abundant supply, and prices and returns reflect that with the capital sitting on the books of everybody. I do believe the advantages that have historically been associated with companies like ours are still strong. And the project at Tengiz, while we wish that the execution was going better than it is and disappointed in the cost and schedule update, there are not many companies in the world that can do a project like that at all. So, I think there are strong advantages there. Our sour gas handling capabilities, our heavy oil expertise continues to be of value. And as we get back to work in the PZ, we will be doing things there that very few other companies can do.

And as I mentioned earlier, we've been hanging in, in Venezuela, which has tremendous potential. And our capability there to help, over time, develop that resource in a responsible way is something that is differentiated. I think there are some historic capabilities that are differentiators.

The other thing I would point to is portfolio. And certainly, as we've talked about many times, I won't belabor it, but our position in the Permian, both from a size standpoint, a quality standpoint, the relative lack of royalty given the fact that's fee acreage and our experience with factory drilling, which is a capability that not everybody has, and we continue to see the benefits of that year after year, is another point of differentiation. I still do believe there are areas that we do differentiate.

Pierre Breber:
If I could build up Mike's answer there. Look, I said in my prepared remarks that our returns are too low, and we're committed to improving them, and we'll share more at our Analyst Day. But I'll also talk about cash flow. We talked about our strong cash flow in 2019Whichever macro environment you want to call it weak or whatever, we're able to do all those things: increase the dividend, fund the capital program, grow production, reduce debt and sustain the buyback program. At our last Analyst Day, we showed that over the next 5 years, we're going to grow cash from ops. We said we're going to keep capital essentially flat. That means we're going to grow free cash flow. I think one of the things that's not fully understood is that the capital efficiency of our program going forward is different than we've seen in the past. So, we're able to grow and sustain cash flows at lower capital than almost any time in the past and certainly better than our peers. And that's what enables us to do the kind of dividend increase that we announced a couple of days ago, sustain a buyback program and still grow the enterprise for the long term.

Operator: Our next question comes from the line of Paul Cheng from Scotiabank

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Paul Cheng (ScotiaBank):
You did an impairment charge, which is quite large. And obviously, that means the decision made at the time, some of the parameters that did not work out. So, what have we learned from this process or this impairment and how your future M&A or project sanctions process has changed?

Mike Wirth:
Yes. Paul, two of the big drivers of that charge were our Marcellus position, which is essentially mostly dry gas. We've got a little bit of Utica, but mostly dry gas. And also, the Kitimat LNG project, which is Canadian gas, that is quite a ways away from the Kitimat site. And both of those, at the time those transactions were entered into, we and the world had a different view on natural gas. I think the Permian and unconventionals have really been a game changer. You look at the prolific gas production in the United States today, the market conditions that we were talking about earlier with Roger, we didn't see those things at the time. So, I do think there's a lesson about testing M&A ideas against scenarios that are not the prevailing view on forward markets. We did that with the Anadarko transaction last year. There's a reason that we like Anadarko from a synergy standpoint. There's a reason we saw a certain value level that we would be willing to transact. And there's a reason we wouldn't go beyond that. That's because commodity markets are hard to predict. And we certainly looked at cases that would have stressed an acquisition because we might experience a different market environment than the one that we premised maybe our central analysis on. Yogi Berra said that predictions are hard, especially when they're about the future. That's certainly true. It's not lost on us. And I would say that's the big lesson from these two is if you're going into the future or into a deal with a pretty strong commodity price, make sure you take a look at what happens if you're wrong and whether or not you'd be happy with it in the scenario where you are wrong.

Paul Cheng:
On the second question, I think Pierre already addressed, return on capital. Last year, you earned 7% at a $64 Brent price, which is lower than the S&P market return, I think. And for most of the investors, they probably think $60, $65 Brent is as much as they're willing to give companies in the long-term assumption. So, you're talking about an improvement. Can you give us some idea that, given the big portfolio you have, where you see the biggest opportunity you may be able to really drive up that return? We're looking at some of the projects, whether it's Tengiz the Future Growth Project or Anchor, and we don't see those projects would be able to improve your overall return at all.

Mike Wirth:
Look, there's no silver bullet on improving returns in a flat commodity price environment. You roll up your sleeves and you get to work on all the little things that cumulatively can drive returns higher. And that's costs, that's margins, that's value chain optimization, it's reliability, it's technology. There's a whole host of levers that you have to be working on. This is what we do in the downstream business every day. And what we have done in the downstream business for decades is you assume margins are going to be worse in the future than they are today. And you've got to find a way to get more efficient and productive with your operations in every little thing that you do That's what we need to do. I'm not satisfied with returns at the level that they are. We're not going to wait for prices to be the answer here. We simply have to get after it. And you'll hear more about this in March. We'll talk more about our plans to improve returns then. But there's not a magic wand here. This is good old-fashioned hard work, and its things that we know how to do. We just have to get after it.

Pierre Breber:
Let me just add, in addition to the cost and margin and value chain and all those efforts. The Permian investments are very accretive to our book returns. We showed in the second quarter that, even in a growing asset, we are investing and

growing in the Permian, that returns are heading to 20% and north of that. So, we do have investments that are accretive to the portfolio. As said earlier, we have capital efficiency that has enabled us to sustain and grow the enterprise at lower capital levels than we have in the past. So, when you take the capital efficiency, plus everything Mike talked about, we intend to increase our returns over time.

Operator: Our next question comes from the line of Jason Gabelman from Cowen.

Jason Gabelman (Cowen):
This follows what Paul just said. Specifically, on Anchor, it seemed like Capex for the project was a bit high. And I was wondering if you could talk about returns. You've kind of danced around it, but maybe talk about returns specifically for that project. And is this one of the more competitive projects in your project queue? And I have a follow-up.

Mike Wirth:
Yes, Jason. If I go back to an earlier period of time, our development costs for deepwater projects were north of $30 a barrel. Anchor is actually ~~south of~~ [correction: around] $20 a barrel, and that includes some investment for new technology that we have to prove out here because we're dealing with deeper reservoir, higher reservoir pressure, 20,000 pounds technology, a little bit of additional export pipeline, which is unique to this project as well. Operating costs have come down from the high teens per barrel down into the range close to $10 a barrel. We've seen significant improvements in drilling and completions performance. And all of those things come together to bring the cost down. I'm not going to give you a specific return number because, frankly, we run these things at different prices and different assumptions around recovery. We look at a range of potential outcomes. But I will tell you, it is competitive in our portfolio. It sets us up for additional follow-on development that will, I think, improve returns. And the technology development unlocks a resource type that we believe holds a lot of potential as we go forward. I don't think we're done in terms of driving these costs down. And in the deepwater, we're going to continue to look to make these projects even more economic.

Jason Gabelman:
When you say unlock the new resource types, is that high-pressure, high-temperature?

Mike Wirth:
Correct, yes.

Jason Gabelman:
Got it. There's not a lot of visibility to your project queue beyond 2025. There's a couple of Gulf of Mexico projects, Permian and TCO, and that's all you've given us. I wonder if you plan on providing more visibility to some of your projects that you have options around. And then attached to that, do you see an opportunity to step into some international projects, maybe with companies that are looking to farm down stakes?

Mike Wirth:
So, we will, in March, lay out a longer view to give you some more transparency. I know that's a question that a number of people have been asking. The one thing that I would suggest is we went through a period of time over the last decade, where, I think, we conditioned ourselves and our investors to believe that the only path to the future was by doing these great, big projects and stacking up lots and lots of them because that's what we were doing at the time. We have a very different portfolio today. We have large tranches of production that are pretty flat and facility limited in Australia LNG, in Kazakhstan. Our unconventionals begin to behave this way as you build up the scale there. And so, at the margin, we have continued to look for the right projects and highly economic projects and, as Pierre said, those that are accretive to returns. But we're not nearly as reliant on those alone to sustain and grow cash flows into the future.

We just have a much more resilient, durable, long-lived portfolio. Grinding away on enormous unconventional positions may not be quite as glamorous as doing the big projects in terms of giving you a lot of things to talk about. But it really drives strong financial outcomes. And it's durable, I think, longer than most people believe. We'll talk about that more in March. We'll talk about other opportunities we have in terms of captured opportunities that people may not be paying much attention to. We'll talk more about our exploration prospects.

And the question on farm-ins, that's always something we evaluate. And if the right opportunities present themselves, we look at those.

Operator: Our next question comes from the line of Biraj Borkhataria from RBC

Biraj Borkhataria (RBC):
The first one is actually just on the base decline. If I look at the figures on Slide 8 and take the base from there, it looks like the base decline was less than 1% in 2019. And I guess, that excludes shales. But I'm just trying to get a sense of whether that figure is relevant and if there's anything funny in the 2019 number that is not applicable going forward. Just some comments around that would be helpful.

Mike Wirth:
Yes. I mean, our base portfolio is large, and there's a lot of different assets in there. There are some things that now are in the base like Jack/St. Malo and Perdido. We've got some of these deepwater projects that are no longer new projects and some of the new investments in there to do next phases of development that give you some growth that offsets some of the underlying decline. But it also comes back to this point I was just making to Jason, a larger percent of our portfolio now is facility limited, not reservoir limited. So, this mental model that reservoir dynamics drive our overall production, the shape of our production profile is one that needs to be calibrated appropriately to a larger and larger portion that does not behave that way. So that results in more stable, predictable production. There's modest investment required to sustain that - facility investment or some new wells. But you look at the brownfield opportunities we have and the ways we're using technology to arrest declines. And base decline is just less in our portfolio than it was a decade ago, and that's not a short-term phenomenon. That's a structural change in how our production looks.

Biraj Borkhataria:
The second question is just on a slightly different tack, but as you guys are seeing in California, I wanted to ask about renewable fuels given the favorable regulation there. We're seeing a number of the U.S. refiners announced expansion projects and renewable diesel, in particular. I was wondering if that's something you're interested in. What you think about the economics? And then if it's attractive to you, what's holding you back from investing in that space?

Mike Wirth:
Well, we've been selling renewable fuels in California for the better part of the last 2 decades, a lot of blending. We've been looking at manufacturing, but we really have chosen not to go into the ethanol business.

On renewable diesel, we've got close relationships with suppliers of renewable diesel. I mentioned earlier in a response to a question, we are making modifications at California refining facilities in order to co-feed biofeedstocks in order to produce renewable diesel. Our view is rather than going into new projects and greenfield developments, we've got existing infrastructure and kit that we have now proven ways to safely and reliably introduce biofeedstocks so it's a more economic way to do it. It takes advantage of existing capital investment, so we're working on that. We are and will continue to be growing in the biofuels value chain.

Operator: Our next question comes from the line of Doug Leggate from Bank of America

Doug Leggate (Bank of America):
Mike and the guys, happy new year to all of you. Mike, we've had some concerns about this particular issue for a second, and it's part of the Permian. I'd like to just get your perspective on it. I realize what you're seeing about returns and the benefit of royalty interest and mineral interest and so on. But by 2023, this is going to be 25% of the company. And when I think about the underlying decline rates on a skew towards NGLs and gas, given the state of U.S. gas market, help me understand why putting that much of your portfolio in high-decline assets and skewing towards U.S. gas is incrementally positive for the overall cash flow capacity of the company.

Mike Wirth:
An individual well is a high-decline asset. The Permian Basin, as you get hundreds and then thousands of wells on production, and you have infrastructure built, the ability to keep that infrastructure full and have it be a very flat production profile at modest incremental investment relative to the production that you're producing is profound. Jay will explain this more in March when we come to New York. But it is a factory. And running a factory, you got certain costs and certain investments in the factory and then you push out to the product of the factory, and that's how to think about the Permian.

The commodity mix, it's 75% liquids. We're 50% oil in our portfolio right now, 25% NGLs, 25% gas. As the volumes continue to grow, we get a lot of oil production, and we take a long view on markets. Pierre mentioned earlier that returns on investment there are greater than 20% and growing. Somebody mentioned earlier, your current returns are at 7% and those need to improve. Well, if you've got opportunities to invest in things that are north of 20%, that's the way to start to lever up returns. We look at the commodity prices on it all, we optimize it. We're moving commodities to markets near and far to add value to that. But these are high-return, long-lived positions, and it is a competitive advantage.

Doug Leggate:
I look forward to what Jay has got to say in March. But just to be clear, those returns are full cycle, including infrastructure and all the plant build out and so on.

Mike Wirth:
And fully loaded with cost, including corporate costs.

Doug Leggate:
Okay. My follow-up, Mike, is more philosophical for the broader energy space. It seems like there's been a kind of an awakening of ESG issues just in this last past 6 months, and particularly this year. More headlines this morning about pension funds just divesting out of fossil fuels altogether. I'm just curious in your position, obviously, as an advocate of the industry, how do you anticipate challenging those kinds of questions over fossil fuel is bad, everything else is good? How does Chevron compete for the incremental investment dollar? And it's an answer I'm looking for some help with because, obviously, it's a challenge for all of us in this business right now.

Mike Wirth:
First of all, we believe in ESG. We have been a responsible operator across E, S, & G for a long, long, long time, and we invest enormously in that. The E is getting a lot of attention right now. And look, over the history of our industry, we and others have reduced the environmental impact of our operations, time and time and time again. We are doing it again today. And we have the scale, the technical capability, the financial capability to be a big part of addressing this challenge. And no one company, no one country, no one industry is going to be the one that solves everything. But collectively, we will respond to the challenge. The world needs more energy. The world needs more affordable energy.

And people in developing economies deserve the opportunity to see their lives improve. And affordable, reliable and ever cleaner energy is essential to improving the quality of life on the planet, which is better today than it has ever been at any point in history and will be better in the future. And we intend to be a part of that solution. We acknowledge that the climate is changing. We acknowledge that human activity and fossil fuels contribute to that. And we acknowledge that we will be part of addressing that as we go forward, so we are investing time, people, money, technology in being part of that solution. I'm an optimist. There's a lot of pessimism that you hear out there. And as you say, over maybe the last 6 months, that drumbeat is even louder, but we saw big challenges in the past. And I'm optimistic that we will be successful again.

Operator: Our next question comes from the line of Alastair Syme from Citibank

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Alastair Syme (Citi):
With the impairment, you're signaling something about LNG. So, the question is, are you happy to tack away completely from LNG? I mean, you've been one of the biggest global investors in the last decade and you clearly created a lot of competency within the organization. So, are you happy to do nothing in effect?

Mike Wirth:
No. We're happy to do things that are competitive and economic, Alastair. We're a big player in LNG. The world demand for LNG will grow over time, and you have to take a long view on these things. Commodity markets get into positions where they get overbuilt. Demand grows in a linear fashion. Supply comes on in stair steps. We're in a position right now where the near-term market fundamentals are a bit tough. But long term, like petrochemicals, like refining, you need to be in low-cost positions that are highly competitive where you've got scale, technology, operating efficiency. Those are the kinds of things we're looking for. And we'll continue to evaluate opportunities to add to our LNG portfolio. Our assessment on the Kitimat project is, given all the other developments out there in the world that, that one was going to be tough to compete versus our alternatives. It's a hard decision to come to, but it doesn't condemn the asset class for us as an investment proposition. We just want to find the very best projects.

Alastair Syme:
Okay. My follow-up, I just wanted to get an update on where you're at in TCO, specifically with any discussions you're having with the government. I'm not sure whether the government has been sort of informed on the cost overruns and where that leaves it.

Mike Wirth:
Yes. The discussions are ongoing. The government is obviously a key stakeholder in this, so our people in-country have been engaged. Jay Johnson will be there next week and both visiting the site and meeting with people from the government. When you go through one of these things, there's a whole series of engagements, and we're in the process on that.

Pierre Breber:
The only thing I'd add to that, Alastair, is that, unlike other agreements in Kazakhstan, our contract is tax and royalty, it's not a production sharing contract. On production sharing contracts, the government reimburses the concessionaires for their costs, which is not the case for tax and royalty. So of course, they're an important stakeholder, but it is a fundamentally different contractual structure.

Operator: And our final question comes from the line of Jamaal Dardar of Tudor, Pickering, Holt, and Co.

Jamaal Dardar (TPH):
Just wanted to touch on the outsized dividend growth that we saw versus previous years here. So just curious on the thought process there. As you continue to shed assets and large MCPs roll off and capital intensity is lowered, just wondering how repeatable outsized dividend growth could be over the long term.

Mike Wirth:
So if you look back at our dividend history, and we were looking back at it not long ago, whether you're looking over multiple decades or over the last decade, we've grown it at a compound annual growth rate of about 6%, so there's a little bit to the upside of that, but we've been lower than that in recent years. And we are well positioned - Pierre talked about our strong cash flow and the capital efficiency that we have now in our portfolio to sustain and grow cash flows with a much lower level of capital investment than, I think, people had become accustomed to over the prior period. We would not have increased the dividend if we weren't absolutely confident that it's sustainable in perpetuity. And just as we said, we intend to sustain our buybacks through the cycle. We intend to sustain strong dividend distribution. Our #1 financial priority, I'll remind you, is to sustain and grow the dividend. This was a signal of confidence in our portfolio. It's a signal of confidence that we can sustain strong cash generation, even in a commodity price environment like the one we've been in and the one we continue to be in. We will talk about this more in March. But we have a very, very strong position to generate cash out of our portfolio, very efficient capital profile going forward, further efficiencies coming on the cost side. We're very confident in the capacity that we have. Decisions are made by the Board. I can't get ahead of the Board on what they may do in the future. But I'll tell you, the Board shares the confidence we have in our cash-generating capacity.

Jamaal Dardar:
And then just a quick one on buybacks. You mentioned the sustainable nature is difficult for us to model the impact of the PSC roll-off, but it seems like ,very temporarily, there could be at strip pricing time periods where ,in order to satisfy the full buyback, maybe you lean into the balance sheet. Just wanted to verify the comfort there, obviously, given where you sit as best-in-class on your debt ratio.

Pierre Breber:
Thanks, Jamaal. If we have to lean on the balance sheet for some point in time, that's okay. We've said we want to sustain it through the cycle. We've never said the buyback has to be funded every single quarter from free cash flow. That's not our expectation. We have the strongest balance sheet in the industry. Our net debt ratio is 13%. Gross debt is 16%. We have the capability to take on some debt. I've talked about, we don't have a target debt range, but certainly, I'd be comfortable [with a debt ratio] higher than we are right now. If we're a little bit low [on debt ratio], that's okay. That's how the math works. So, if we generate cash at surplus to our top 3 priorities, which is to pay the dividend, invest in the business and have a strong balance sheet, we'll return that in the form of share buybacks. But we also want to keep that ratable and sustainable, so we don't want to ramp up buybacks because we want to be able to essentially dollar cost average and do it through the cycle. So, the short answer is yes. There'll be times we'll lean on our balance sheet, and our balance sheet has that capability. Our intent is to sustain the buyback through the cycle.

Wayne Borduin:
Thanks, Jamaal. With that, I'd like to thank everyone for your time today. We do appreciate your interest in Chevron and everyone's participation on today's call. Jonathan, back to you.

Operator: Ladies and gentlemen, this concludes Chevron's fourth quarter 2019 earnings conference call. You may now disconnect.