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EDITED TRANSCRIPT

CVX - Q3 2013 Chevron Earnings Conference Call

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OVERVIEW:

CVX reported 3Q13 earnings of $5b or $2.57 per diluted share.

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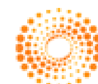

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PRESENTATION

Operator

Good morning, my name is Jonathan and I will be your conference facilitator today. Welcome to Chevron's third-quarter 2013 earnings conference call.

At this time, all participants are in a listen-only mode. After the speakers' remarks, there will be a question-and-answer session and instructions will be given at that time.

(Operator Instructions)

I would now like to turn the call over to Vice President and Chief Financial Officer of Chevron Corporation, Ms. Pat Yarrington. Please go ahead.

Pat Yarrington - *Chevron Corporation - VP & CFO*

Thank you, Jonathan. Welcome to Chevron's third-quarter earnings conference call and webcast.

On the call with me today are Joe Geagea, Corporate Vice President and President, Gas & Midstream, and Jeff Gustavson, General Manager, Investor Relations. We will 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. We ask that you review the cautionary statement on slide 2.

Slide 3 provides an overview of our financial performance. The Company's third-quarter earnings were $5 billion, or $2.57 per diluted share.

Return on capital employed for the trailing 12 months was 15%. Our debt ratio at the end of September was 11%.

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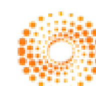

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In the third quarter we repurchased $1.25 billion of our shares. In the fourth quarter, we expect to repurchase the same amount.

Though not shown on this slide, I would like to call attention to our track record on shareholder returns. We are in first place on total shareholder return for the 3 year, 5 year, and 10 year periods, compared to our peer group of global integrated energy companies.

Turning to slide 4, cash generated from operations was $10 billion during the third quarter, and approximately $25 billion year to date. The third quarter was the strongest cash generation quarter this year. Adverse working capital effects noted earlier in the year continued to abate.

Importantly, third quarter also saw stronger operating performance in both our Upstream and Downstream businesses. Capital and exploratory expenditures were $9.6 billion during the quarter, and $26.4 billion year-to-date.

I would like to make it clear that major resource acquisitions, stemming from our business development activities, are not included in our annual budget targets. We have found the success rate, timing, and pricing for this effort to be too uncertain to effectively include in our annual budgeting and Board approval process for C&E.

Because we have been very successful this year in our resource acquisition effort, taking up acreage and project opportunities in Canada, Australia, and the Kurdistan region of Iraq, we anticipate we will close the year with C&E outlays above our planned level. While there are still some large uncertainties on timing, we presently anticipate our 2013 C&E investments will be around 10% or so higher than our original target for the year.

At quarter-end, our cash balances exceeded $18 billion. As total debt balances were identical in size, we ended the quarter in a neutral net cash, net debt position. Confirming what I have said previously, the Company continues to move toward a more traditional net debt structure.

Jeff will now take us through the quarterly comparison. Jeff?

Jeff Gustavson - *Chevron Corporation - General Manager IR*

Thanks, Pat. Turning to slide 5, I'll compare results of the third quarter 2013 with the second quarter of 2013. As a reminder, our earnings release compares third quarter 2013 with the same quarter a year ago.

Third-quarter earnings were $5 billion, about $400 million lower than second-quarter results. Foreign exchange movements accounted for more than the overall decrease in earnings, worth almost $600 million of the decline. The strengthening of the US dollar in the second quarter, and the weakening of the US dollar in the third quarter caused a significant swing between the two periods.

We moved from a net positive foreign exchange position in the second quarter of $300 million to a net negative position at nearly the same amount of third quarter. Without this element, our earnings performance this quarter would actually be better than the prior quarter.

Upstream earnings were up $143 million, reflecting higher liquids realizations and liftings, mostly offset by unfavorable foreign exchange effects. Downstream results decreased $386 million between quarters. Lower margins and unfavorable foreign exchange effects, partly offset by higher volumes, drove the decrease. The variance in the Other bar largely reflects an unfavorable swing in corporate tax items during the quarter.

On slide 6, our US Upstream earnings for the third quarter were $57 million lower than second quarter's results. Higher realizations increased earnings by $90 million, driven largely by a rise in crude oil prices, partially offset by the fall in natural gas prices.

Lower production volumes decreased earnings by $30 million, mainly due to maintenance activity in the Gulf of Mexico, partly offset by higher production in the Permian. The Other bar reflects a number of unrelated items, including higher DD&A, and higher exploration expenses.

Turning to slide 7, International Upstream earnings were $200 million higher than the second quarter. Higher realizations increased earnings by $430 million.

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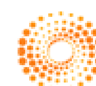

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Average liquids unit realizations increased by 11%, consistent with the increase in average Brent spot prices between quarters. The timing of liftings across multiple countries increased earnings by $90 million. At the end of the quarter, we were in a slightly over-lifted position.

And unfavorable swing in foreign currency effects decreased earnings by $465 million. The third quarter had a loss of about $190 million compared to a gain of about $275 million in the second quarter.

The Other bar reflects a number of items. Favorable tax effects, gains on asset transactions, and lower operating expenses were partially offset by higher exploration expenses.

Slide 8 summarizes the quarterly change in Chevron's worldwide net oil equivalent production. Production increased 3,000 barrels per day between quarters. New wells in our Agbami and Usan projects in Nigeria, additional production from the Delaware Basin in the Permian, as well as volumes associated with Angola LNG increased net production by about 22,000 barrels per day.

Planned maintenance activities decreased production by 14,000 barrels per day during the quarter, most notably in the UK, Trinidad, and Thailand, with a partial offset from less maintenance activity in Australia. External constraints hurt third quarter production by 10,000 barrels per day, primarily due to a mid-quarter lightning strike in Thailand, which severely damaged and necessitated the shutdown of a customer's gas processing plant. This in turn curtailed our Thai gas production.

The base business and other bar includes the impact of normal field declines, cost recoveries, and the impact of price effects on the entitlement volumes. Production for the first three quarters of 2013 averaged just over 2.6 million barrels a day, below our initial full-year production guidance of 2.65 million barrels per day.

Several factors have affected our year-to-date production results. First, Angola LNG's ramp-up of production has been slower than anticipated.

Second, turnaround activity across various locations has been more extensive than originally planned. A final contributing factor relates to the damage at the gas plant in Thailand.

We expect volumes to be higher in the fourth quarter as production is restored, following maintenance-related downtime during the third quarter, and as new production comes online. For the full year, we expect to come in around 98% to 99% of our original production target.

Turning to slide 9, US Downstream earnings improved by $111 million between periods. Higher volumes increased earnings by $55 million, primarily due to our Richmond, California refinery running at normal capacity for the full quarter. Lower refining and marketing margins decreased earnings by $95 million, driven by rising crude costs.

Reduced industry crack spreads also reflected improved supply conditions and higher plant utilization rates, following the end of second-quarter maintenance activity. Lower operating expenses increased earnings by $30 million, primarily due to lower environmental charges.

Greater gains on miscellaneous small asset sales improved earnings in the third quarter by $60 million. The Chemicals and Other variance primarily reflects the absence of planned and unplanned downtime at CPChem's Port Arthur and Sweeny plants in the second quarter.

On slide 10, International Downstream earnings decreased by $497 million between quarters. Higher plant utilization rates boosted volumes and increased earnings by $30 million in the third quarter.

Refining and marketing margins were lower by $220 million. Rising crude costs, continued soft product demand, and oversupply in the Far East weakened industry crack spreads, while price lag effects, mainly for jet fuel and naphtha in Asia impacted marketing margins. Timing effects represented a $140 million negative earnings variance between quarters, driven largely by the revaluation of inventory. The swing between quarters was primarily due to rising crude prices during the third quarter, compared to falling crude prices during the second quarter.

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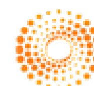

Foreign currency swings reduced earnings by about $115 million. Third quarter had a loss of approximately $85 million, compared to a small gain of $30 million in the second quarter. The Other bar includes a number of unrelated items, including various tax items, and higher shipping costs.

Slide 11 covers All Other. Third-quarter net charges were $522 million, compared to $350 million in the second quarter, an increase of $172 million between periods. Adverse corporate tax items resulted in a $219 million decrease to earnings between quarters.

Our overall year-to-date effective tax rate, at just around 40%, is trending a little lower than in recent years. As you know, in any one period, this overall rate can be influenced by many factors, including jurisdictional mix between Upstream and Downstream, jurisdictional mix within Upstream, foreign exchange, and asset sales transactions. Corporate charges and other items were $47 million lower this quarter.

Year-to-date net charges in the All Other segment were $1.3 billion at the end of the third quarter. We believe our quarterly guidance range of $400 million to $500 million for the All Other segment is still appropriate going forward.

Joe is now going to provide an update on our LNG marketing activities. Joe?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

Thank you, Jeff, and good morning, everyone. I would like to spend a few minutes talking about the LNG market, and our LNG portfolio.

So turning to slide 13, I will start by grounding you quickly on the global demand outlook for energy. The world economy is growing, driving increased demand for all forms of energy, and much of this growth is in Asia, where people increasingly aspire for a better quality of life, and achieving this aspiration does require stable, secure, and affordable energy supplies.

Total world energy demand is forecast to increase 30% by 2025 from today's level. Natural gas demand is projected to grow even more, by about 40% by 2025, and LNG demand growth is expected to be even greater.

Starting to slide 14, LNG demand has already doubled since 2000, and it is predicted to double again by 2025. Meeting this demand would require three elements. Maintaining the reliability of existing supply, delivering current LNG projects under construction, and investing in the construction of new LNG capacity.

Even if the first two elements are well in hand, that still leaves an opportunity of around 150 million tons per year of new projects to be sanctioned. Now, many buyers are counting on the United States to make up the shortfall, with pricing linked to Henry Hub.

Even if you believe the most optimistic predictions of new US supply available for export, there is still a projected shortfall of more than 50 million tons in 2025. And more reasonable predictions of US exports suggest a gap of around 100 million tons in 2025. So the US alone will not bridge this forecast demand supply gap, and thus we believe new supply needs to come from multiple sources.

Now developing these supplies will also take time, whether that's for permitting and construction of US LNG export terminals, or for exploration, appraisal and development of new producing regions, such as East Africa. Building and maintaining LNG facilities is technically challenging, capital intensive, and requires significant expertise.

The last 35 LNG projects developed globally took on average of over 18 years to deliver that LNG to market, although we do acknowledge that completion times are improving. Additionally, capacity utilization rates for LNG facilities in production have only averaged about 85% in recent years. Geopolitical instability, resource availability, and unplanned turnarounds have resulted on average in roughly 35 million metric tons of the existing nameplate capacity being unavailable at any given time.

Turning to slide 15, while we have seen growth in global energy trading and expect that interregional trade of LNG will continue to increase, we believe that global gas markets will remain regionally distinct over the medium to long term. This is mainly due to the high cost and relative lack of infrastructure to transport and store gas globally.

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While two-thirds of the world's oil is shipped by tanker, only 10% of the world's current natural gas supply is shipped as LNG. Now this is forecast increased to 14% by 2025. We believe the majority of this LNG will continue to be delivered under long-term contracts.

The traditional LNG importing countries of Japan, Korea, and Taiwan have no interconnecting pipeline infrastructure, and virtually no indigenous energy resources, and therefore rely on LNG to meet almost all of their gas demand. Only five years ago, 17 countries were importing LNG. Today, 26 countries are doing so, and this is expected to increase.

So let's move to slide 16, where I'd like to focus more specifically on US LNG exports. Many analysts forecast that US LNG exports should reach approximately 50 million tons per year by 2025, equivalent to around 11% of the world LNG demand, and about 8% of domestic US gas demand.

At these levels, US LNG exports would only represent a small share of the global LNG market. Greenfield LNG projects are unlikely to be developed outside of the United States, unless a significant portion of the offtake is committed under long-term contracts, with robust pricing that underpins the financial investment required to monetize these resources.

A common perception is that Henry Hub linked pricing will mean landed LNG prices in Asia will be significantly less than other world sources. We think that is not automatically a given. US liquefaction costs are likely to rise, as more projects compete for resources, including engineering contractors, fabrication yard space, and project financing.

In addition, growing demand in the United States for new petrochemical projects, power plants, exports to Mexico and the transportation segment, will mean new demand pull on the same supply base. Coupled with weather and storage effects, this could easily lead to increased price strength and volatility for Henry Hub. In order to ensure that sufficient supplies do get developed, there needs to be cooperation, alignment, and understanding between LNG buyers and suppliers.

This is helpful when buyers diversify their energy mix, maintain a geographically diverse LNG portfolio, recognizing that no one region, including the United States, can meet all expected demand, and finally take equity positions in LNG projects, to ensure the right projects are built in the right places, for the right price. Now, we have seen this formula work in Gorgon and Wheatstone, and we're confident the same will be true for Kitimat.

Turning to slide 17, I would like to now talk about our LNG sale commitments. From a portfolio perspective, we believe it is prudent to leave around 25% of volume for placement on the spot market for operational flexibility. However, at the individual project level, this ratio may very.

For example, on Gorgon, we are 65% committed. We are still prepared to increase volumes under contract, however, Gorgon is scheduled to come online when a time when limited new supplies are expected, so we are confident in being able to place uncommitted volumes into the market.

On Wheatstone, 85% of Chevron's equity LNG is now committed on a long-term basis. In addition to the Gorgon and Wheatstone foundation projects, we have made good progress this year with buyers for LNG from our Indonesia Deepwater Development, or IDD.

For our unsanctioned projects, including IDD, Kitimat, and Gorgon Train 4, we are targeting to have around 70% committed under long-term contracts, by the time we reach our final investment decision. Once achieved, we will end up with our desired portfolio objective of having 75% of our LNG production sold through long-term contracts.

Turning to slide 18, I would like to close by showing you how Chevron is well-positioned to become a major LNG supplier by the end of this decade, based on WoodMac estimates. With the projects under construction at Gorgon and Wheatstone, and with our existing equity shares at Angola LNG and Australia North West Shelf, we will be one of the top 10 LNG suppliers in the world. If we include Kitimat and Gorgon Train 4, we will potentially move into the top five.

In summary, we see strong LNG market fundamentals supporting our growing LNG portfolio, which should allow us to deliver strong future cash generation for many years to come. I will now turn it back to Pat.

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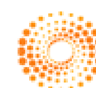

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Pat Yarrington - *Chevron Corporation - VP & CFO*

Okay, thank you, Joe. Now, let's take a look at the latest update on our LNG projects.

The Gorgon project is over 70% complete. We continue to make good progress in all fronts. In early October, we installed the third of five gas turbine generators.

To date, 14 of the 21 LNG Train 1 process modules have been installed, 3 are in transit, and the remaining are scheduled to follow in fairly rapid succession. Work on the jetty is progressing. We now have 43 of the 56 jetty caissons installed, including those needed to support all key structural elements.

We have recently reached mechanical completion of the domestic gas pipeline, in preparation for operational readiness by year-end. Offshore pipe lays are complete on the Io-Jansz 30-inch pipeline. And finally, three wells at the Io-Jansz field are ready to flow gas, and seven wells are completed at the Gorgon field.

Wheatstone is proceeding per plan, and is now over 20% complete. We continue to transform the site with ongoing earthwork and good progress on establishing critical infrastructure. Construction continues on the materials offloading facility, and we completed our first permanent foundation concrete pour in September.

Site preparation continues with about 19% of our 23,000 piles driven, including the commencement of the LNG tank pile driving. Platform construction is over 43% complete, and we have received critical platform equipment, such as the power transformers and process vessels. We just completed our micro-tunnel boring under the shoreline, in preparation for the offshore installation of the truck line.

Now, we have posted several updated photos of progress made at both Gorgon and Wheatstone on our investor website, located at Chevron.com, and I invite you to take a look at those.

For Kitimat, front-end engineering continues on plan. We remain focused on early earthworks at the LNG plant site, where construction on the office, camp industrial site, and service road is ongoing.

Key activities for the Pacific Trail Pipeline are obtaining necessary permits, building roads, and securing right-of-way access. LNG marketing activities and engagement with potential foundation customers are underway. The timing of the final investment decision will be determined by our ability to secure sufficient LNG offtake agreements with our customers.

Turning now to slide 20, I would like to share some highlights of the strategic progress we have made during the quarter. We signed binding long-term sales and purchase agreements with Tohoku Electric Power Company in Japan, to supply just under 1 million tons per year of LNG, for up to 20 years. As Joe noted, this brings total volumes committed to customers in Asia on a long-term basis to 85% for our Wheatstone project.

Continuing with the Australian theme, we recently announced the acquisition of two deepwater exploration interests located in the Bight Basin, off the southern Australian coast. These are very large blocks, with significant exploration potential, and further reinforces the importance of Australia to Chevron's global growth strategy.

In Canada, we successfully completed an initial 12-well exploration drilling program in the liquids-rich program of the Kaybob area of the Duvernay shale play. Initial well results were very encouraging, with average initial production rates in excess of 1,200 barrels of oil equivalent per day. Both of these developments are consistent with our focus on early entry opportunities, which have the potential to generate the most value for our shareholders.

We also had a major milestone in our Downstream and Chemicals business. CPChem announced Final Investment Decisions for its US Gulf Coast petrochemicals project.

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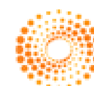

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This project includes construction of a 1.5 million metric ton per year ethane cracker, as well as two new polyethylene facilities, each with an annual capacity of 500,000 metric tons. This is an attractive project, one that takes advantage of existing infrastructure and advanced feedstock. Plant startup is planned for 2017.

Turning now to slide 21, I would like to close by highlighting our continued strong performance, particularly in our Upstream business. Our 2013 year-to-date Upstream earnings margin was $23.33 per barrel. Based on these year-to-date results, we continue to lead our direct peer group by a wide margin, we are almost $5.70 per barrel ahead of our closest competitor.

This is a position we have now held for 15 consecutive quarters. We also led on this important metric at the six-month mark by over $4.25 per barrel, against a wide range of E&P companies. These peer-leading financial results are directly related to the quality of our investment decisions, and the strength of our portfolio.

We appreciate you listening in this morning, and your interest in the company. I would now like to open the microphones. Joe and I are happy to take your questions.

We do have a full queue, so please limit yourself to one question and a single related follow-up, if that is necessary. We will certainly do our very best to see that we get all your questions answered. So Jonathan, please open up the lines for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question comes from the line of Ed Westlake from Credit Suisse. Your question please.

Ed Westlake - *Credit Suisse - Analyst*

Thanks very much for getting Joe on the call, so I will start with an LNG question. I am up late tonight, and I keep getting these stories from Australia on my iPad, which obviously bang around the market, and people are very worried about the LNG jetty, or whatever it is, something else, with the project. Maybe give us color on how you're feeling about the start-up date and maybe if there are any penalties if the date slips back in time, what is the killer date to get Gorgon onstream?

Pat Yarrington - *Chevron Corporation - VP & CFO*

Thanks Ed for the question. I think we have been pretty upfront about acknowledging some of the challenges that we have had earlier.

We talked previously about logistics challenges, labor productivity, and weather challenges. We have solved, for all practical purposes, the logistics challenges, and in fact, we have asked for and have received additional laydown space on the island, and so we are able to now build material and inventory on Barrow Island.

Productivity, I would say, is improving on all fronts, but there are still some areas that still need to improve. We are impacted by weather. We had a heavy rainy period back in June, but right now, we're in the good weather period and are making very good progress each month.

I think we are moving into a critical phase from a schedule standpoint on the project. We talked about getting all of Train 1 modules onto the island. That is proceeding pretty much as planned.

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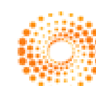

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I think largely they will be here by year-end or shortly into the new year. Maybe one that will be mid-quarter next year.

What's important next is the mechanical, electrical, and instrumentation work and construction -- contractor work on those activities is ramping up on the island now. But there are still uncertainties that exist with the project of our size, and our challenge every day is to mitigate the risks, find the risks, mitigate the risks as they arrive.

But the jetty, I think we tried to say, all the critical elements of the jetty, the main critical elements of the jetty, those that support the structural elements, are on plan. Right now, we are in the process of finalizing our budgets for the year, and should there be any reviews during that, that suggest a material change, other than what we have said previously, we will certainly bring that to your attention. But I do not have anything more to offer.

Ed Westlake - *Credit Suisse - Analyst*

Thanks.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

Let me address your question on the marketing side. I would like to say that our customers are our partners, so they fully understand the project challenges.

I would also say that Gorgon is not coming up all at once, it is one train at the time, so that gives us time to work with our partners, with our customers on accommodating their needs. We have those discussions ongoing all the time. I cannot address specifically what is in our contract with respect to penalties, as you can appreciate these are commercial elements, and I cannot address those.

Ed Westlake - *Credit Suisse - Analyst*

Thanks very much.

Operator

Our next question comes from the line of Evan Calio from Morgan Stanley. Your question please.

Evan Calio - *Morgan Stanley - Analyst*

Thanks for the LNG commentary, as well as addressing that CapEx question. Staying with Gorgon, Joe, can you update us on how the FEED on Train 4 is progressing, and what is the interplay on trains 1 and 3? Their progress, and the ultimate decision upon expansion, meaning do your partners need to see more final Gorgon cost estimates before committing to the expansion, and albeit, it's a significantly lower unit cost expansion.

Pat Yarrington - *Chevron Corporation - VP & CFO*

Yes, I will take the question around Train 4. I think we continue to work with our partners. We are all interested certainly in seeing this continue to progress. I think all of the JV partners are interested though, in seeing Train 1 come up and seeing progress on 2 and 3, et cetera.

Everybody wants to get an understanding of the cost structure. I also think that people want to get certainty around the fiscal and regulatory regime, and as you know, there's been a change of government in Australia. So a little bit of settling down and stability there would be appreciated. Those factors are going to be taken into account.

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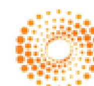

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I also think it is fair to say that the cost structure in Australia is different now than it was when Train 1 was taken, trains 1 through 3 were taken to Final Investment Decision back in 2009. The cost structure has elevated, and I think it's fair to say, that has put at risk some of Australia's kind of global competitiveness.

So from a Chevron standpoint, we are going to look at Train 4 and we are going to assess it under those new conditions, and we're going to look at that, relative to other opportunities that we have got in our portfolio, and look for that next investment to compete with other opportunities. Obviously, Train 4 does have certain brownfield economic advantages to it, but we need to take those advantages, lay in the new macro conditions that we see in Australia, and take a look at the whole portfolio activity. Having said all of that, we are continuing on with environmental approvals for Train 4.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

So maybe I will add a bit of color commentary also, because the marketing is essential to Train 4, and all the reasons that Pat has mentioned, I would also say that the LNG market has different dynamics, as well. Our job is to continue to find customers for Train 4, which we continue to do. We believe the offerings of Train 4 are different than the offering of our other projects, like Kitimat.

Train 4 is an expansion, is a Brownfield expansion, Train 4 is exposure to Australia. Train 4, however, does not have equity, unlike Kitimat, where we're offering equity. So it caters to a different set of customers, and in our view, from a marketing perspective, it is really not competing with Kitimat, and I think that's important for us to say.

Evan Calio - *Morgan Stanley - Analyst*

Thank you, so the follow-up is that -- does that mean that potential debottlenecking of trains 1 through 3 is something that could potentially precede a Train 4? I mean, I understand there are three different tranches of potential expansion. Does that change the debottlenecking opportunity to move that forward, or is that still something that would follow, if it did in fact follow?

Pat Yarrington - *Chevron Corporation - VP & CFO*

Yes, I mean, Evan, debottlenecking is always something that you would do, as an ordinary course of activity. Oftentimes, it has the very highest economics associated with it, so that will be taken into account in our normal planning process.

Evan Calio - *Morgan Stanley - Analyst*

Okay, great. I'll let somebody else, thank you.

Operator

Our next question comes from the line of John Herrlin from Societe Generale. Your question, please.

John Herrlin - *Societe Generale - Analyst*

Yes just two quick ones. With the Duvernay wells, about how much were they running? I know it's science time in its early days, but I'm wondering about approximate cost.

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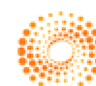

Pat Yarrington - *Chevron Corporation - VP & CFO*

Are you talking approximate well costs?

John Herrlin - *Societe Generale - Analyst*

Well costs.

Pat Yarrington - *Chevron Corporation - VP & CFO*

That is not a number that we want to give out at this point in time.

John Herrlin - *Societe Generale - Analyst*

Okay, that is fine. Next one is on LNG. Are you surprised at all that on the demand side, in terms of customers, that they haven't built more physical gas storage, in Asia, and do you think that will change as the LNG market builds up more?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

That is a very good question John, this is Joe here. It is going to take time to for them to get there.

Clearly, there is some capacity with the regas terminals, and we're seeing that in Thailand, we're seeing that in Singapore, but remember that market is huge. So a significant amount of storage has to be made available for it to really make a difference. I think we may get there eventually, but I see a slow pace to get to that point.

John Herrlin - *Societe Generale - Analyst*

Okay great. Thank you.

Operator

Our next question comes from the line of Doug Leggate from Bank of America - Merrill Lynch. Your question, please.

Doug Leggate - *BofA Merrill Lynch - Analyst*

If I could try two also, please. Joe, first of all, can you remind us what the contract resets look like on your baseload marketing, for Gorgon in particular? Maybe when you're addressing that question, if you would talk a little bit about whether the issue around Henry Hub pricing is really more about delinking, and in the event -- oil for example went to $150, but led to actually depressing the current price, and I have a follow-up.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

I will start by saying that most contracts that are of that length, 20 years, for them to be sustainable and to be win-win for both buyer and seller has reopeners on them. Without getting into specifics, these reopeners are meant to really make sure that the pricing formula continue to reflect the market. What I can tell you, is that all of our projects are paced, that we are not going to see major renewal for a big portion of the volume, all in one year. We are being very careful in pacing these renewables over time, because again, that is in our interest and in the buyers' interest, to spread that renewal timing over a longer frame than just having them all occur at the same time.

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Back to your questions on Henry Hub. There are two elements to it. We have been public in saying that LNG that comes out of the United States, made in the United States is perfectly okay for it to be priced out of Henry Hub. LNG that is made in Australia, East Africa, or Canada, it's a harder proposition to see why you would introduce a regional market reference to those markets, so that's been very difficult.

In terms of breaking the oil linkage, I will tell you that for the last four years, the industry has learned to operate within an oil framework that saw oil prices go up $140 and go down to $20. I submit to you that within these traditional framework, you can introduce S-curves, you can moderate slopes, there are a lot of other levers that actually work to prevent LNG from becoming very unaffordable in the regions where affordability is becoming an issue.

So I think we can address those excursions that could be harmful from an affordability point of view, within a traditional framework, without necessarily going to something unproven that could also be a lot more volatile. We have also said that one way for people to get a better attenuation on price is for them to get into the equity side. That clearly gives them direct exposure to the upstream side, to the whole value chain, and effectively you are getting an attenuation to pricing, because you're getting the whole value chain and benefits from that. So hopefully that helps.

Doug Leggate - *BofA Merrill Lynch - Analyst*

It does a lot, thanks, Joe. My follow-up is quicker, we all watch the unit earnings trends very strongly, the earnings trends you've had for quite some time now. But whether we want to look at earnings or cash flow, the focus is earnings.

My question is, your DD&A runs about $6 lower than your peer group, and that appears to be trending higher. So when you have all of this non-producing capital coming online from these new projects, can you give us some feel as to how the DD&A trend will look? And I'll leave it at that, thank you.

Pat Yarrington - *Chevron Corporation - VP & CFO*

Right, so Doug I think you should expect, we have seen and you should expect the trend to continue, higher charges for DD&A. Certainly, that's the pattern we've seen over the last couple of years, it's the pattern that we have seen looking at 2013 versus 2012, and it is the expectation that I would have going forward for 2014, and it is a direct reflection of the capital investment programs that we have had underway, and as we bring those new projects online, you see rate increases associated with that.

Doug Leggate - *BofA Merrill Lynch - Analyst*

All right, I'll leave it there. Thanks, Pat.

Pat Yarrington - *Chevron Corporation - VP & CFO*

But Doug, I would say, it's important, even with that, we still have the leading earnings per barrel margin, and we have the leading cash margin.

Doug Leggate - *BofA Merrill Lynch - Analyst*

I'm just trying to figure out what the future trend is going to look like when these projects, come up, Pat.

Pat Yarrington - *Chevron Corporation - VP & CFO*

I appreciate that.

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Doug Leggate - *BofA Merrill Lynch - Analyst*

Thank you very much.

Operator

Our next question comes from the line of Paul Cheng, from Barclays Capital. Your question, please

Paul Cheng - *Barclays Capital - Analyst*

Two somewhat related questions, one for Joe, and one for Pat. For Joe, when we look at Kitimat, if you can give us some idea of what is the competitive position relative to building a LNG plant in Kitimat, and operate there, which is a pretty remote area, and later could be an issue, compared to in Australia, where you have a lot of operations, or in the Gulf of Mexico, where you don't have a lot of operation.

So that's the first one. Pat, do you want me to give you the second one first?

Pat Yarrington - *Chevron Corporation - VP & CFO*

Sure.

Paul Cheng - *Barclays Capital - Analyst*

If I look at, this is not an issue in the near term, but your current cash flow essentially just barely covers your CapEx. And so at what point now, of course when you have zero net debt, that is not an issue today, but theoretically, at a management standpoint, at what point do you start questioning whether you want to continue borrowing money to buy back stock, and at what point will that continue, once that you eliminate the share buyback, that you will have to relook at your CapEx program?

Pat Yarrington - *Chevron Corporation - VP & CFO*

Okay, good question.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

I will go first on the Kitimat question, and it's a very good question. I will start by talking a little bit about the resource base.

If you look at our acquisition of that resource base, we are very, very pleased with the entry price. So we also know that we have a huge resource base in both Liard and the Horn River.

That resource base sits right at the gate of North Asia, where we continuously see increased demand. So strategically, it is very well-positioned for our North Asia buyers, and our buyers see that, and that is the value proposition we've been communicating to them.

They also see in Kitimat two partners that have complementary skills, they are very aligned, and very committed to the project. They see a federal government and a provisional government that are supportive and understand the opportunity.

They see a country that is very much in favor of exports, and tilting toward Asia. They see a project with export permits in hand, and a clear line of sight on a pipeline and a transportation solution.

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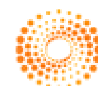

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Now you did say something about the labor costs. I will tell you though, if we are the first out of the gate, we will have an ability to attenuate that, versus being the last one coming in to develop the project.

And finally what we tell our buyers, this is a great opportunity for them to participate through equity and the whole value chain, and in doing so they really get direct exposure to North American gas pricing. All of those are good value drivers for any buyer in north Asia. They are getting it, I think we're getting good reception, and obviously time will tell in our ability to sign contracts, but we are very encouraged by what we see, and the value that Kitimat can offer to those buyers. Now go back to Pat for the capital outlook.

Paul Cheng - *Barclays Capital - Analyst*

Joe, before that, from a cost standpoint, do you -- because you know a lot about Australia, and I presume you know quite a lot about Gulf Coast. Is developing cost and operating cost of Kitimat is going to be competitive with Australia, but cheaper than the Gulf Coast or any insight you can provide?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

It's too early for us. I remind you that we signed the transaction in February of this year, and we became operator in July of this year.

We are really getting on top -- there are two things here that we need to be careful on, is project development and execution, which is really what we're focused on, and secondly the marketing, and they have to go hand-in-hand. I would tell you though, the freight advantage that we see in Western Canada clearly is something in favor of Canada, compared to Gulf Coast exports.

Pat Yarrington - *Chevron Corporation - VP & CFO*

Paul going back to your question, I want to start with the priorities that we have always put out there in terms of uses of cash. Dividends first, reinvesting in the business, taking care of our balance sheet, and then share repurchases really come at the very tail end of that. And you are right, we are in a period, right now, where our capital requirements are high.

Just to remind you, we have got five LNG trains under construction, that is a very significant component. We do not have and do not in the forward-look that we will have anything as lumpy as that, or as sized as that.

So we know 2013 is a high C&E year. We have said in the past the 2014 will be a high C&E year. George referenced last time on the call about a flattening that will occur. So we do see that the uniqueness of our capital spent period right is not something that we see coming forward in two or three years.

At the same time though, we do fundamentally believe our greatest value proposition for our shareholders is finding and investing in the right resources, and developing the right projects. So we will continue to invest in the business, and so you see us doing that, in terms of resource acquisitions that I talked about earlier.

We try very hard to balance this returns and growth equation here, and we've been very successful. The decisions that we have made and we believe the new resource acquisitions that we have made for the future, for growth, 2020 and beyond, are excellent projects. So we believe we are putting that equation together quite nicely.

I guess the other thing that I would say is, when you bring in new resource acquisitions, like we have done with Kurdistan, or Cooper Basin, or Kitimat, et cetera, when you are adding those elements to your portfolio, it does mean that you reprioritize your portfolio, and certain things probably fall toward the bottom. These would be more mature assets, less competitive in our portfolio, believe they have a potentially a spot in someone else's portfolio, and that is where your asset sale or portfolio optimization component increases.

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We've been very good at doing that in Downstream, you've seen us do all that restructuring in Downstream. Joe has overseen a fair amount of restructuring occurring in our Midstream area, and I think you can expect some additional asset sales now coming forward from Upstream.

Paul Cheng - *Barclays Capital - Analyst*

Is there some form of matrix that you look at from a financial net debt to capital, or net debt to EBITDA you would look at? Once you reach a certain level of the share buyback, we'll say maybe they come to a halt?

Pat Yarrington - *Chevron Corporation - VP & CFO*

We obviously are interested in maintaining our AA status, credit rating status. We're not interested in infringing upon that at all, so we look at that as the limiting factor. But frankly, Paul, we are such a long way away from that at this point, it is not a limiting component.

Paul Cheng - *Barclays Capital - Analyst*

Thank you.

Operator

Thank you our next question comes from the line of Faisel Khan from Citigroup. Your question, please.

Faisel Khan - *Citigroup - Analyst*

Two questions. First, on the LNG facility in Canada or potential LNG facility in Canada.

Can you discuss the merits of owning the entire integrated asset? Why not move into a more asset-light model where a utility-like company owns the liquefaction facility, you own the resource, and you market the gas, and charter the ships? It seems like it's a very large piece of invested capital, there's a lot of companies out there, especially in Canada and the US that have the ability to finance this stuff at a much lower cost of capital.

And my follow-up is, it seems like building a pipeline from the yard in Horn River even to Kitimat is very expensive. There is a lot of depreciated pipe all the way from there down to the Gulf Coast that has a lower invested capital base.

Why not ship the gas down there, and sign up with one of these other facilities that are sort of ramping up? That's a little in left field, but maybe you can help me answer those.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

That's not in left field at all, Faisel, good question. Let me tell you we are not building up pipeline from the field to the LNG facility. We are clearly leveraging existing trunk lines that currently run, and they are operated and owned by others.

The piece that we are building is a link from the trunk line to our facility. I call that our umbilical, and that is very essential for us to actually control that, to control the feed going into the LNG facility.

So where we can, we are leveraging other facilities, infrastructures, processing plants could be another place where we leverage as well. So we are adopting some of what you are suggesting.

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When we do this we always look at the strategic fit of the asset. Is it essential for us to control it from a commercial point of view, is it essential for flow assurance to our facility, those are normally governing criteria for us to decide whether we want to own the interconnecting framework, the same thing about ships.

We can sell FOB, as well, and we don't have to build ships, but sometimes we have to build ships to ensure flow assurance on the back end of the LNG facility. The name of the game is really to get the molecules that we just acquired at a very attractive price, in the Horn and Liard to the market, and maximize our returns and we look through that whole thing in details.

And the other options also we are looking at, from lowering the capital investment, we are asking other equity partners to come in, and by farming in for buyers, clearly we are lowering the capital exposure. So we are looking at all of that to basically address the element of the question that you brought, Faisel.

Faisel Khan - *Citigroup - Analyst*

Okay, and then the pipeline gas. If you could pipeline all this gas down to the Gulf Coast on what is basically all this depreciated pipeline, whether it's Alliance or Northern Border, and then down to -- down in GPL to the Gulf coast.

I mean, the invested capital of those assets is far lower than these pipelines that TransCanada and Spectra are talking about building to supply that gas to the Canadian west coast. I mean, is that an opportunity where you can move that resource down to the Gulf Coast and export it out of the Gulf coast, and with the Panama Canal opening up, it seems like an asset-light model, but I don't know.

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

Food for thought, thank you, Faisel.

Faisel Khan - *Citigroup - Analyst*

Okay, fair enough. Thanks.

Operator

Thank you our next question comes from the line of Pavel Molchanov from Raymond James. Your question, please.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Two questions on your unconventional gas exposure. US gas production was up almost 5% year-over-year. Is that primarily legacy Atlas acreage?

Pat Yarrington - *Chevron Corporation - VP & CFO*

I think there is both an Atlas component, as well as a newer Permian Delaware Basin component to that.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Okay, fair enough. And then onto Europe. Lots of headlines recently involving countries where you are operating, or thought about operating in. Lithuania, Romania, et cetera. Any status update you want to provide on how you're thinking about that?

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Pat Yarrington - *Chevron Corporation - VP & CFO*

I think we tried to say, right from the get-go, that this would be a long-term development opportunity, and that it would take several years really to understand how the overall play could develop. We do think, if it works, and if it is proven up, then there is enough here to potentially build a business, but we are just in the very early stages of exploration, and so I do not want to get -- I don't want to leap into far, too soon, with implications here.

We are active in Poland, we have drilled four wells. We've got 3D seismic underway as well there. In Romania, we are picking up seismic activity. Ukraine, we are still interested in having the PSA signed, and we are hopefully getting closer on that.

So we continue to make progress. It will be dependent upon the local governments and the local communities wanting to have us be there, and so that has been a challenge. It is an exploration play, so I think we need to give it time to mature.

Pavel Molchanov - *Raymond James & Associates - Analyst*

All right, I appreciate it.

Operator

Our next question comes from the line of Roger Read with Wells Fargo. Your question, please.

Roger Read - *Wells Fargo Securities - Analyst*

I guess I would like to, on the upstream side, focus a little bit more on the cost side of things. I mean obviously, it was a good quarter in terms of realizations on the top line, but you talked a little bit of earlier about DD&A being an issue. Is there anything else, maybe particular to the third quarter, from an operating cost standpoint, that is not recurring? I know maintenance is an issue sometimes, but I was just seeing if you could help us there, and think about how that unfolds in 2014 and 2015?

Pat Yarrington - *Chevron Corporation - VP & CFO*

I think from a cost standpoint, so exploration was heavier in the third quarter than the second quarter, but if you look on a year-to-date basis, it's pretty much in line with what we had seen previously. We are seeing higher industry costs, you referenced that, I think that's just a general trend that has been evident.

But also, maintenance in the third quarter was a little bit heavier, per planned as well as some unplanned as well. So I think those are the factors that I would call your attention to.

Roger Read - *Wells Fargo Securities - Analyst*

And in terms of any thoughts on 2014 and 2015, are we seeing trends here? I agree with you that the industry is seeing higher costs, but are there any trends specific to Chevron that we should think about? Or even another way of asking it, as the LNG projects come on, are we going to see that as a significant impact, maybe lowering operating cost?

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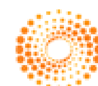

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Pat Yarrington - *Chevron Corporation - VP & CFO*

Yes, I do not think that the unique in Chevron's operations, going forward, that I would suggest. I think I will defer on the LNG operations side of things. I am not in a position to comment about what op expense looks like in 2015 and 2016 at this point.

Okay, I think we have time for one my question.

Operator

Certainly. Our final question comes from the line of Allen Good from Morningstar. Your question, please.

Allen Good - *Morningstar - Analyst*

Good morning everyone. Just a couple for Joe on LNG. You have been pretty detailed on the merits of Canadian gas, relative to Gorgon, and relative to the US. Should we go ahead and take it that exporting natural gas out of the Gulf Coast does not fit competitively within Chevron's current LNG portfolio?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

Well, you're making too many assumptions right there. We are focused on Kitimat for now, and again, we have opportunities in Australia. We're not ruling anything out at this stage, but at the same time, I am not prepared to tell you that we will not look at opportunities anywhere else in the world. For now, we're focusing on Canada.

Allen Good - *Morningstar - Analyst*

Okay, and finally, you mentioned the appeal of the equity availability in Kitimat for some of your potential partners. Is there a minimum equity stake that Chevron would like to retain in Kitimat, or vice versa, a target that you would like to sell down as a portion of equity in the project?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

We have not put any number out there, obviously, it's up to the buyer also to indicate interest. We kind of like a number in our mind, in terms of where we will end up, but it's really a function of where the buyers are. We're flexible, and remember, we have a partner as well, and we have to consult with them in terms of where they would like to end up. The gate is open, though, for the buyers to tell us what they think. I do not know that we have indicated externally what that number is, but we are open to entertain the buyers' ideas.

Allen Good - *Morningstar - Analyst*

Okay thanks. If I get one more quick one. You make a great convincing case that the demand for LNG will be out there. Do you see any threats in the supply side, though, that could potentially disrupt the potential long-term economics for LNG projects?

Joe Geagea - *Chevron Corporation - Corporate VP & President, Gas and Midstream*

In fact, I see the threat in the opposite direction. I see that threat as the longer it's taking us to enable projects to reach FID, and you fast-forward it four or five years, how long it takes to build them, this market can only go up.

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And that is not really what the buyers would like, and that's why our plea with the buyers have been, we need to enable supply to come to the market, because we have not been anything on the demand side that is managing that carefully. We see more subsidy, we see nuclear out of the energy mix, we see shale gas development in a lot of places, slower outside the United States.

All of that points to more need for LNG, and I look at how many projects are actually reaching FID outside the United States, I don't see a whole lot, and that can only mean problems down the road.

We have seen that play out in the past, back in 2007 there was an estimate of about 75 million tons of LNG that would hit the market in 2014. As we said today, there's only 10 millions tons that will come in 2014. So we have got to crack this equation, both from the supply side and the demand side, and the longer we see projects delayed from reaching FID, I think the price equation gets more difficult.

Allen Good - *Morningstar - Analyst*

Okay, thanks for that.

Pat Yarrington - *Chevron Corporation - VP & CFO*

Okay, thank you. Before we close out the call, since we did not get a question on Ecuador, I would like to provide our investors an update on this matter before we close out here. It is a very important matter.

As you're probably well aware, there have been several recent positive developments related to this ongoing litigation. Earlier in the year several key witnesses, financiers, and other associates, including an Ecuadorian judge involved in the case, publicly denounced and exposed numerous examples of the blatant fraudulent tactics used by the plaintiffs lawyers during the trial.

But more recently, an international tribunal, convened under the authority of the US Ecuador Bilateral Investment Treaty, and administered by the permanent Court of Arbitration in the Hague found that the settlement and release agreements between the Government of Ecuador and Texaco in the mid-to-late 90s released Texaco Petroleum Company from any liability for all public interest or collective environmental claims. Now, this is the definitive ruling on the single most important legal issue in the case, and it was made by an impartial tribunal in Hague, where Chevron had picked one arbiter, the government of Ecuador had picked one arbiter, and we both had agreed on the third, and it was a unanimous ruling.

Importantly, this ruling confirms that the claims against Texaco were not valid, and should not have been brought in the first place, and it also signifies that efforts to enforce the Ecuadorian judgment, which the plaintiffs have so far unsuccessfully attempted in both Canada and Argentina, that those are in direct violation of national and international laws.

Now, separately, a couple of weeks back, on October 15, the US trial began in New York related to Chevron's civil lawsuit against the Lago Agrio plaintiff, and several of their lawyers, consultants, and supporters, alleging RICO violations, violations of the Racketeer Influence and Corrupt Organizations Act. Trial proceedings in this New York lawsuit are expected to last a few more weeks.

So, we are encouraged by these recent developments, but at the same time, we expect to need to continue to defend our position and defend our assets well into the future, before final resolution becomes available to us.

So with that, I will close off finally here, and again thank you for your interest in the Company and your time here this morning. Good day to everyone.

Operator

Ladies and gentlemen, this concludes Chevron's third quarter 2013 earnings conference call. You may now disconnect.

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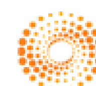

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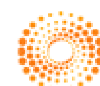

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