

# FINAL TRANSCRIPT

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## CVX - Q3 2010 Chevron Earnings Conference Call

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## CORPORATE PARTICIPANTS

**Pat Yarrington**

*Chevron Corporation - VP & CFO*

**Jeanette Ourada**

*Chevron Corporation - General Manager, IR*

**Mike Wirth**

*Chevron Corporation - EVP, Downstream and Chemicals*

## CONFERENCE CALL PARTICIPANTS

**Evan Calio**

*Morgan Stanley - Analyst*

**Doug Leggate**

*BofA Merrill Lynch - Analyst*

**Paul Sankey**

*Deutsche Bank - Analyst*

**Paul Cheng**

*Barclays Capital - Analyst*

**Mark Gilman**

*The Benchmark Company - Analyst*

**Faisal Khan**

*Citi - Analyst*

**Pavel Molchanov**

*Raymond James - Analyst*

**John Herrlin**

*Societe Generale - Analyst*

## PRESENTATION

**Operator**

Good morning. My name is Sean and I will be your conference facilitator today. Welcome to Chevron's third quarter 2010 earnings conference call.

At this time all participants are in a listen-only mode. After the speaker's remarks there will be a question-and-answer session and instructions will be given at that time. (Operator Instructions) As a reminder, this conference call is being recorded.

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

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Thank you, Sean. Welcome to Chevron's third quarter earnings conference call and webcast. On the call with me today are Mike Wirth, Executive Vice President of Downstream and Chemicals, and Jeanette Ourada, General Manager of Investor Relations.

Our focus today is on Chevron's financial and operating results for the third quarter of 2010. We will refer to the slides that are available on Chevron's website.



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Before we get started, please be reminded that this presentation contains estimates, projections, and other forward-looking statements and I ask that you review the cautionary statement on slide two.

Slide three provides an overview of our financial performance. The Company's third quarter earnings were \$3.8 billion or \$1.87 per diluted share. Our third quarter 2010 earnings were flat compared to third quarter 2009. Compared to the second quarter 2010 earnings fell 30%; Jeanette will discuss the sequential earnings variance shortly.

Return on capital employed for the trailing 12 months was about 16%, total debt at the end of the quarter was \$10.6 billion, and our debt ratio was 9.4%. Total cash at the end of the quarter was \$14.5 billion and this was after a \$550 million pension contribution. Third quarter was our strongest cash generation quarter since third quarter 2008.

As you will see in the remainder of our presentation, our third quarter earnings were negatively impacted by several large items which had no corresponding impact on cash. A prime example here is foreign exchange. The quarter's earnings included almost \$370 million in foreign exchange losses which were simply balance sheet translation effects.

In July our Board of Directors approved a new share repurchase program. As previously announced, we will begin repurchases in the fourth quarter here. We are targeting a repurchase rate between \$500 million and \$1 billion per quarter, and in the fourth quarter we expect to repurchase \$750 million of our shares.

Jeanette will now take us through the quarterly comparisons.

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**Jeanette Ourada** - *Chevron Corporation - General Manager, IR*

Thanks, Pat. Turning to slide four, I will compare results of third quarter 2010 with second quarter 2010. As a reminder, our earnings release compares third quarter 2010 with the same quarter a year ago.

Third quarter earnings decreased \$1.6 billion from the second quarter. Results for all segments dropped between periods.

Upstream earnings were \$978 million lower, largely due to an unfavorable foreign currency variance and higher exploration expenses. Third quarter Downstream results were \$410 million lower, driven by adverse foreign currency and timing variances. The Other bar largely reflects an unfavorable swing in corporate tax items.

On slide five our U.S. Upstream earnings for the fourth quarter -- third quarter were \$144 million lower than the second quarter's results. Crude oil realizations reduced earnings by \$55 million. Chevron's U.S. crude realizations fell about \$2 per barrel between consecutive quarters, slightly more than the 2% change in WTI spot prices. Natural gas realizations were flat between periods.

Higher operating expenses decreased earnings by \$35 million between periods, primarily due to impacts from the Gulf of Mexico drilling moratorium. The Other bar represents a decrease of \$54 million, which is comprised of a number of unrelated items including higher asset impairment charges.

Turning to slide six, international Upstream earnings were down \$834 million compared with the second quarter. Realizations reduced earnings by \$40 million with lower liquids realizations partially offset by higher natural gas realizations. Our average liquids realizations decreased 2% between quarters, in-line with the decrease in average Brent spot prices. Natural gas realizations improved 8% between quarters.

Lower liftings decreased earnings by \$115 million. For the third quarter we were underlifted by over 3%. Bringing the year-to-date position to slightly over 1% underlifted.



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Higher exploration expense reduced earnings by \$210 million due to well write-offs in Turkey and Canada. An unfavorable swing in foreign currency effects lowered earnings between quarters by \$350 million. The second quarter had a gain of about \$100 million compared to a \$250 million loss in the third quarter. The Other bar reflects a number of unrelated items including higher depreciation and lower pipeline and sulfur earnings.

In the interim update we forecast \$200 million of discrete items in the international Upstream segment. These items include an out-of-period depreciation adjustment and an equity redetermination of a field covering multiple leases. The depreciation adjustment covered multiple years and was not material in any year. These items were either non-cash or cash neutral.

Slide seven summarizes the quarterly change in Chevron's worldwide net oil equivalent production. Production decreased 8,000 barrels per day between quarters. Price changes had a modest effect on volumes under production sharing and variable royalty contracts in the third quarter increasing production about 2,000 barrels per day. The average WTI price declined about \$1.75 per barrel between quarters.

Base business production decreased 30,000 barrels per day between quarters, mainly due to planned turnarounds in Europe and normal field declines, partly offset by higher demand in Thailand.

As shown in the green bar, contributions from major capital projects increased third quarter production by 20,000 barrels per day primarily driven by lower planned shutdown activities at Tengiz in Kazakhstan.

Before I turn to the Downstream results I would like to note that our Upstream adjusted earnings for the quarter were \$14.65 per barrel. Based on preliminary competitor results announced to date, we continue to lead our peer group on this metric for the fifth consecutive quarter.

Turning to slide eight. U.S. Downstream earnings fell \$84 million in the third quarter. Indicator margins reduced earnings by \$60 million; Gulf Coast refining indicators margins fell by 20% due to tempered demand growth and high inventories. West Coast refining indicator margins were relatively flat. Actual margin capture and higher volumes added a small increase to earnings.

The Other bar consists of several unrelated items, including unfavorable mark-to-market effects on open paper, partly offset by better core trading results.

International Downstream earnings were also lower, decreasing \$326 million from second quarter's results. Higher margins and volumes benefited earnings by \$50 million with each contributing about half the variance. Improved margins in Asia and Canada were partly offset by declines in Europe.

Volumes were also higher in the third quarter, in part due to the absence of second quarter planned maintenance at our Cape Town refinery.

An adverse swing in foreign currency effects reduced earnings by \$250 million. Second quarter included a \$130 million gain while third quarter had a \$120 million loss. Timing effects represented \$180 million negative variance between quarters, reflecting inventory revaluation and unfavorable mark-to-market affects on open paper tied to underlying physical positions.

In the second quarter WTI prices moved down from the beginning to the end of the quarter, generating a paper gain. In the third quarter WTI prices moved up from the beginning to the end of the quarter, generating a paper loss. The Other bar is comprised of several unrelated items, including better core trading results and a favorable OpEx variance due to the absence of the second quarter planned turnaround at Cape Town.



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Slide 10 covers All Other. Third quarter net charges were \$361 million compared to a net \$108 million charge in the second quarter, an increase of \$253 million between quarters. An unfavorable swing in corporate tax items resulted in a \$259 million variance. Corporate charges were modestly lower in the third quarter.

On a year-to-date basis the segment has net charges of approximately \$850 million. We believe our quarterly guidance range of \$250 million \$350 million for net charges in the All Other segment is still appropriate going forward.

Mike is now going to provide an update on our Downstream business. Mike?

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**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Thanks, Jeanette. I'm pleased to have the opportunity to update everyone on the progress we have made in restructuring Downstream and improving performance.

Just a quick comment on the results Jeanette just covered. We have had a good quarter and, in fact, a good nine months, especially given the amount of change underway. Our financial results have improved markedly from last year due to good execution in the base business and steady progress on the improvement initiatives we've undertaken. And while the benefits from some of those improvements are reflected in our results, others are only beginning to appear now and the full effects should be seen in the coming quarters.

I'm especially proud of our continued strong performance in the areas of safety and reliability. Through nine months Downstream is experiencing its safest year ever. In terms of reliability, the utilization of our refinery units continues to be high as it has been for the last several years.

I'd like to share some details on our restructuring efforts and major capital projects, both of which are right on track. Please turn to slide 12.

As I told you in March, our focus is on improving returns. I committed to delivering operational excellence in our base business while high grading our portfolio, reducing costs, and improving revenues. At the end of September, a new, leaner organizational structure was in place. Every employee knows their status in the new organization. We expect to meet our target of 2,000 workforce reductions by the end of 2010.

We've captured \$275 million in improvement in our refining system versus our 2008 Solomon baseline. Most of this comes through cost reductions, including reduced contractor counts and less employee overtime due to increased work productivity and renegotiated contracts for materials, chemicals, and contract labor. We are also increasing refinery profitability through improved energy efficiency, better yield optimization, and tighter blending tolerances to reduce specification giveaway.

Turning to slide 13 -- excuse me, I have got a little more here. We have also taken action to high-grade our portfolio to create a simpler footprint and improve focus and efficiency.

We completed the previously announced market exit from 12 states in the Eastern U.S. We have closed the sale and transitioned operations of four terminals and are continuing negotiations on nine others. Sales agreements have been signed for our businesses in eight African countries. Some of these could close as early as the fourth quarter and the balance will close in 2011.

Earlier this month, we announced the sale of our minority interest in the Colonial Pipeline Company to KKR. You'll see the financial impact of this sale in fourth quarter results.



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And divestiture efforts are in progress for assets in Europe, the Caribbean, and select countries in Central America. Data rooms are currently open and are being accessed by potential bidders, and we're close to finalizing a sales agreement for our businesses in the Western Caribbean and parts of Central America. We will continue to keep you advised as these transactions materialize.

Now turning to slide 13. Capital discipline is an essential part of our commitment to improved returns. Our 2010 capital budget is 23% lower than it was in 2009 and I expect we'll come in even further below that number. Having said that, we do have a few key projects underway that I would like to update you on.

The Ras Laffan Olefins Complex, which is a greenfield, world-scale ethylene cracker in Qatar, was started up successfully in the second quarter of this year. In Yeosu, South Korea, a new heavy oil hydrocracker will lower feedstock costs and increase high-value product yield. This project was mechanically complete in June, two months ahead of schedule, and came on stream in the third quarter.

The Pascagoula continuous catalytic reformer project, which will enhance reliability and performance, has reached mechanical completion and is in final commissioning. And the Saudi Polymer Company project, another greenfield, world-scale ethylene cracker with derivative units, is on track for start-up in 2011.

I would like to say a few words about the two chemical projects. Chevron Phillips Chemical Company has developed these Middle East ventures based on an attractive feedstock terms, world-class economies of scale, strong partner relations, and excellent project execution. They will be coming online into what we expect to be the beginning of an up cycle and they should perform well in the years ahead.

So in summary, I'm pleased to report the progress we have made on our restructuring to improve performance and to deliver on our commitment to improve returns. With that I'd like to turn it back over to Pat.

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Thanks, Mike. Now turning to slide 14, I'd like to close with a recap of Chevron's strategic highlights during the third quarter.

We continued our record-setting trend in safety performance. Mike provided you with an update of our Downstream restructuring, which is on track and progressing well.

In our Upstream business, we had a number of accomplishments in the third quarter. We continued our exploration success in Australia with natural gas discoveries at Acme and Brederode. These discoveries will further contribute to expansion opportunities for Gorgon and Wheatstone.

We acquired exploration acreage in several new prospective deepwater basins -- off-shore Liberia, China's Pearl River Mouth Basin, and the Turkish sector of the Black Sea. These are large blocks and the combined total acreage, exploratory acreage exceeds 20,000 square miles or 53,000 square kilometers.

And finally, we sanctioned two deepwater projects in the Gulf of Mexico. The Tahiti-2 project will drill two additional producing wells and three additional water injection wells to extend Tahiti's peak production and increase ultimate recovery. We received a permit to drill a water injection well at Tahiti and began drilling there with the Discoverer Clear Leader in late September.

We also authorized the \$7.5 billion Jack/St. Malo development. This will be Chevron's first operated project in the Lower Tertiary. The development is a semi submersible, floating production facility hub in 7,000 feet of water with multiple subsea tie backs.

The Jack/St. Malo fields are estimated to contain combined total recoverable resources in excess of 500 million oil equivalent barrels. We do not expect to book proved reserves for this project in 2010.

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We are pleased that the drilling moratorium has been lifted. This is the first step needed to return thousands of people to work and to begin drilling back in the Gulf.

The second step is its reemergence of an efficient permitting process. We have submitted one deepwater drilling permit and we have an active exploration and development drilling program planned for 2011. We are actively trying to understand and address any remaining issues that the regulators may have. We remain hopeful that drilling approvals will be received in a timely manner.

In summary, our base business is healthy and robust. We are on track to meet our revised production target for the year. We're meeting key milestones in progressing our major capital projects and our Downstream is delivering on its restructuring commitments.

Our cash generation is superb giving us the flexibility to reinvest in our business and return immediate value to our shareholders through a growing dividend stream and share repurchases. We are certainly executing on all of our key strategies.

So that concludes our prepared remarks. And now I'm happy to open up the floor for any of your questions. Sean, please open up the line.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Evan Calio, Morgan Stanley.

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### Evan Calio - Morgan Stanley - Analyst

Good morning, guys. Thanks for taking my call. Since Mike is this quarter's special guest, I am going to start with a question on the Downstream. Mike, could you update us on the sale process for Pembroke or how it's shaping up, interest level exceed expectations and when you expect it might close?

And then any update on Hawaii. You hadn't mentioned Hawaii in terms of either sale, closure or kind of renegotiation of that contract there.

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### Mike Wirth - Chevron Corporation - EVP, Downstream and Chemicals

Okay. You bet, Evan. I'll start with Pembroke and remind you that there are also additional European assets included with that -- some fuels marketing in the UK, Ireland, Spain, the Canary Islands, aviation, etc.

We started out with a long list of bidders earlier this year and got some strong indications of interest. We subsequently narrowed that to a shorter list of preferred bidders and are in the process now of working with them to finalize their proposals. As I mentioned in my comments, the data room is open and being accessed by these bidders.

They have all conducted site visits and are deep into their due diligence. We expect to see their final proposals later here in the fourth quarter.

I can tell you the interest has been strong. This is a good refinery. It's a 210,000 barrel a day facility with good complexity, a natural deepwater port that makes the logistics just excellent for bringing in advantaged crude and also for exporting products into global markets. And the marketing assets are attractive as well.

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So it's a good asset and a good package. It doesn't fit with our portfolio, which is really focused into North America and Asia, but for others who have a better fit it's attractive. And we have got an excellent workforce there.

So we've seen strong interest from what I consider to be good-quality bidders and the process continues. We'll have more to say on that as we receive final bids and then move into negotiations.

Relative to Hawaii, as I think I mentioned in March, we had reviewed the continued operation of that facility and alternatives to convert it to a terminal. We concluded that there wasn't really a value-creating move in conversion to a terminal so we have continued to operate as a refinery. We have restructured several contracts, including one critical large fuel oil contract, there to improve the profitability of the facility and we have found more optimization opportunities within our system.

So, the performance of the refinery has improved since I saw you in March. Having said that, we are still looking at our alternatives here to return the maximum value to our shareholders and so other alternatives are still under consideration. We'll have more to say about that as we reach any critical decisions.

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**Evan Calio** - Morgan Stanley - Analyst

That is great. That is great; thanks, Mike. If I could, one more question moving to the Upstream. I know the CapEx level elevated in 2009 when you brought on a series of material projects that were almost 500,000 barrels a day in Blind Faith, Agbami, Tengiz, Tahiti, Frade and a few others. Should we expect another CapEx increase off your 21.6 year-on-year with the big project queue into 2013 through 2015?

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**Pat Yarrington** - Chevron Corporation - VP & CFO

Yes, that is a good question and we are not prepared at this point to give you a new number for 2011. We customarily do that. We are reviewing the plans right now and we customarily do that after we have Board approval for the plans and so that will be sometime later this year or early in January.

But it's clear we are investing at a healthy pace. We do have strong cash flows and we have low leverage and the breadth and depth of our queue is extraordinary, and this gives us a lot of flexibility. Those factors combined give us a lot of flexibility in project selection.

You mentioned, and we do have, these large projects on the horizon -- Gorgon, Wheatstone, deepwater -- and we were successful here in this last quarter in particular in picking up some new resource opportunities. And those resource opportunities will require further evaluation.

So I do think you will see our outlays go up, but our projects are staggered. And as we sift through our opportunities we always do an affordability overlay and in that overlay we take into account commodity prices, industry costs, and different scenarios. And so this ensures in the end that our C&E program is affordable, even in less robust scenario situations, and that only the best projects get funded.

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**Evan Calio** - Morgan Stanley - Analyst

Okay, that's great. I will leave it there. Thanks.

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**Operator**

Doug Leggate, Bank of America Merrill Lynch.



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**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Thank you. Good morning, everybody. Mike, I'm also going to take advantage of you being there and, Pat, if it's okay, I have a follow up for you also.

Mike, on your comments about expecting the beginning of an up cycle, I'm just kind of curious if you could give us a little bit of color as to where your head is on the environment right now.

And if I may just jump on the Hawaii question, could you elaborate a little bit on the fuel contract? I think I heard you say you already secured it. I was not aware the regulator had approved it yet, but if you could give some color on that.

And as I say, I have a follow up for Pat, please.

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Okay. Yes, so, my reference to projects coming on into an up cycle was specifically directed at the two chemicals projects that I made reference to. We've actually seen a pretty good chemicals market this year, more so in the first half than in the second half where margins have been softening as we have seen some additional capacity come on-line.

But as we move through the next few quarters, where we could continue to see that softening trend hold as economies really gain traction, out into the medium term the chemicals cycle looks as if it's poised for an upturn. And so we're very pleased with the performance of our chemicals affiliates, both at Chevron Phillips Chemical and also in Korea with GS Caltex and are wholly-owned specialty additive chemical company.

We think the fundamentals in that sector are encouraging out into the medium term. If you are -- I want to be sure that I differentiate that from the refining segment where I don't share nearly as bullish a view.

In the refining sector we continue to see pretty tepid demand growth. Some parts of the world certainly showing decent demand growth, others are not. The continued incursion of mandated alternative fuels, fuel efficiency, and the addition of refining capacity, particularly in Asia and the Middle East, will contribute, we believe, to an overhang in refining capacity for years to come.

And so, on the refining side of our business we are prepared for tough conditions for several years out into the future and that is why the focus on self-help that I have been talking about in recent discussions with you.

In Hawaii, the contract, the fuel oil contract, has been renegotiated. I have to tell you, Doug, I'm not current on the state of regulatory approval. I know it's been submitted for regulatory approval but I will have to have a Jeanette get back to you with a specific answer on that because I just don't recall.

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Thanks, Mike. I have a quick one. What is Chevron's stance on Prop 23?

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Well, we have a -- we've taken a neutral stance on Prop 23, Doug. It's an interesting question. I mean this is the first time to my knowledge that voters are actually going to speak on climate regulation.



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I think the proposition really raises a legitimate issue about the impact on the economy and on jobs. Carbon regulations will not come for free and California has real economic challenges. And California cannot materially impact global CO2 emissions on its own. So I think it's a very legitimate question that has been put forward through this proposition.

Having said that, we have taken a neutral position on Prop 23. We have a different footprint in this state than perhaps some others do and this is our home. We continue to work closely with the Air Resources Board and the governor's staff to seek reasonable market-based solutions for carbon reduction in California. And we're looking at how we would meet AB 32 in the most technically feasible and cost effective manner.

It's tough because the final regulations are not complete so there is still some uncertainty out there. But in the broader context we have been working to address climate change really through a variety of different strategies; higher energy efficiency which we've been working on really for the last two decades. We spent a lot of money on R&D and improved technologies focused on renewables and energy efficiency looking for promising and profitable opportunities in things like our Weyerhaeuser venture, and then supporting flexible and sound policies.

So we are preparing ourselves to deal with climate regulation and deal with it in a business context, but we have stayed neutral on Prop 23.

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**Doug Leggate** - *BofA Merrill Lynch - Analyst*

All right. Thanks, Mike. My quick follow-up; this is for Pat. Pat, hopefully it's a quick one.

Exploration spend was up in the third quarter. If you could -- it seemed to be light in the first half of the year. If you could give us an idea how you would expect that to trend. And also DD&A stepped up in the third quarter; if you could help us understand what was going on there that would be great. Thank you.

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Sure, Doug. The exploration expense certainly did move up in the third quarter. Jeanette referenced two significant well write-offs in Turkey and Canada.

I think if you look at us year-to-date 2010 versus year-to-date 2009 you will still find, however, that our 2010 expense factor is about 25% or so lower than year-to-date 2009. This tends to be a very lumpy item for us. Some of these wells are very expensive wells; in some of these circumstances it is pure wildcatting and so it's very hard for us to predict.

On DD&A you also saw a step up; Jeanette also mentioned some of the retroactive adjustment that we had there. Again, year-to-date 2010 versus 2009 we are seeing higher impacts associated with rates but also higher production.

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**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Okay, so that DD&A rate is probably a go-forward, a good go-forward number, Pat, or is the trend still higher?

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**Jeanette Ourada** - *Chevron Corporation - General Manager, IR*

Well, we did mention the -- it was an out of period adjustment --

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Right, right.

**Jeanette Ourada** - *Chevron Corporation - General Manager, IR*

-- so the vast majority of that increase would not be going forward.

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Great, thanks a lot.

**Operator**

Paul Sankey, Deutsche Bank.

**Paul Sankey** - *Deutsche Bank - Analyst*

Hi, guys. Again, I would like to echo, Mike, thanks for making the effort to come on the call. We appreciate Chevron tending always to have an executive available to answer questions. Thank you.

Mike, a very specific one, having said all that, which is how much CO2 do you emit in California, I wondered? And, secondly, could you talk a little bit more about the Asian oil market in general? I know you guys have a huge footprint there. I would just be very interested by any observations you have on how market dynamics are shifting, both from the supply side in terms of refining capacity availability and crude use and also on the demand side? Thanks.

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Yes, Paul, I would -- on your first question on carbon emissions in California, I would point you to our corporate responsibility report where we make a lot of disclosures. Everything that we publicly disclose on carbon is in there. I don't have a copy in front of me right now. We've got both Upstream and Downstream operations here, so I would just point you to that.

On Asia, it is certainly the most optimistic part of the world in terms of economic growth. I have recently been over there and visited multiple countries. I will tell you it is not homogeneous by any means. There is a strongly growing Asia that is really represented by China primarily but also a number of other economies; Singapore is exceptionally strong, Vietnam is strong. So there's a very rapidly growing Asia where we see strong demand for our products.

There is a modestly growing Asia, which is still pretty attractive, and that is markets like Malaysia, Pakistan, Taiwan where we see growth. It's good growth but it's not as strong as you would see in China and some of the others.

Then there is a part of Asia that doesn't look a heck of a lot better than the U.S. Growth is negative still in Japan and fairly flattish in places like South Korea or the Philippines or Thailand.

And so we really have exposure to a number of those markets and we have the ability to try to optimize our refinery production and our supply activities into those markets that have the strongest growth characteristics, the best margin opportunities, and try to mitigate some of the exposure to the weaker markets and optimize there.



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So I think increasingly, we all need to be paying attention to Asia in our business because it is really where the growth will occur. But the key point I think is that there are many different countries in Asia, and their economic circumstances vary pretty dramatically.

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**Paul Sankey** - Deutsche Bank - Analyst

How are you planning the supply side in terms of shutdowns? I'm thinking of Japan, maybe met some loss of capacity in China, and also low utilization rates perhaps amongst some of the players?

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**Mike Wirth** - Chevron Corporation - EVP, Downstream and Chemicals

Yes, you know, we certainly have seen some announced intentions to shut-in capacity in the countries you reference, Japan and China. You know, frankly, I think these tend to occur at the margin. And as you look at some of the teakettle refineries in China or some of the changes in Japan, you also have to look at some of the big new builds in China, the capacity that is pretty fresh, new in India. Vietnam has brought on new refining capacity. So net, the capacity is going up, not down, in Asia.

And even with some economic utilization cutbacks and turnarounds, Asia is long and the world is long. So I think we really do need demand growth to steadily chew into that. Perhaps some projects will be delayed that haven't started construction at this point, and some slow and gradual rationalization. But as I mentioned earlier, we're not banking on a rapid rationalization of the industry and a return to tighter supply and demand balances anytime soon.

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**Paul Sankey** - Deutsche Bank - Analyst

Great, thanks. Then if I could have an Upstream one. You mentioned there is an impact, obviously, from the moratorium in the Gulf of Mexico but you have submitted a permit. I was wondering if you could be a little bit more specific about the volume impact that that is having right now. I guess it's an accelerating effect with decline rates.

And I just wondered if we could somehow get a sense of when you think you may be able to resume. For example, how long it would be before you resumed activity after you received a permit or if there is any way you can frame for us how long you think it will be before you resume? Thanks a lot.

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**Pat Yarrington** - Chevron Corporation - VP & CFO

Sure, Paul. In terms of the impact in the quarter, really let me just talk about the second half of the year. We are estimating a volume impact somewhere less than 10,000 barrels a day and, of course, we've got operating expense impacts that Jeanette referenced as well. Those -- with the moratorium lifted, as soon as we get back to having permits actually authorized then of course those effects become muted.

It's very hard, Paul, for us to say exactly how long a return to -- how long it will take for the permits to be authorized. We're working very aggressively with the BOEM to understand what their uncertainties are and to try to work through that very, very quickly. As I did mention, we did -- we are doing the Tahiti water injection well so there is some progress, but I think it's going to be slow. We're hopeful in the next several weeks, few weeks, couple of months that we will have a better indication of how long exactly it will take to get through the permitting process.

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**Paul Sankey** - Deutsche Bank - Analyst

Is there a very serious potential impact on volumes for next year, at least as a portion of your Gulf of Mexico volumes? Say, for example, if there was no more activity in the next year.

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Paul, it's really too early for us to give an indication of that. I mean, we're right in the midst of trying to get things back to work.

**Paul Sankey** - *Deutsche Bank - Analyst*

Yes, good luck with that. Thank you.

**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Thank you.

**Operator**

Paul Cheng, Barclays Capital.

**Paul Cheng** - *Barclays Capital - Analyst*

Hey, guys. If I could have two questions from Mike and maybe one for either Jeanette or Pat.

Mike, on -- I think historically you guys looking at Asia as a major core market for you because of the growth. But on the other hand, as you indicate, there's a lot of new capacity coming up and a lot of time there may be driven by certain national [priority] and so while the demand is growing, capacity seems to be growing even at a faster pace. And so does that change your view of the attractiveness of Asia as your core market?

The second question is on the chemical. Saudi Arabia, it looks right now they are already short in the domestic gas supply. Do you have a long-term feedstock gas price contract for the next 20 years on that if you -- I don't need to know the exact term, but if you can give us some idea of that. I mean how sustainable is your cost advantage on there?

And also in chemical, you -- do you believe that the joint venture structure is the best on a going-forward or that it will be better there to be owned by the single parties?

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Okay. So I think there were three questions there. The first one --

**Paul Cheng** - *Barclays Capital - Analyst*

I am trying to squeeze into two.

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Okay, that was well done, Paul. On the attractiveness of Asia, I think you really have to look at this in a broad sweep of time. Long-term this is -- the next several decades I think are the decades where Asia will move into a very prominent role in the global economy and there will be attractive opportunities to participate in that.

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We aren't going to jump into projects just to be in Asia and invest there. We need to have profitable investments, and particularly in the downstream and chemicals business we are keenly aware of the realities of a margin-based business and supply and demand. And so we'll be very thoughtful in terms of anything we would do.

Certainly, as I said, over the near to medium term we are expecting some pretty tough sledding. And, frankly, you are seeing others say the same things and some begin to behave that way as projects have slowed down and the like.

And so we're not going to plow into things just to be there. We have got a good strong position right now. We can optimize that position and look for the right kinds of opportunities over time to profitably participate in that growth. And so I think it's still an attractive market to us but we are going to be prudent in terms of how we participate in growth.

On your question relative to Saudi Arabia and feedstock for our ethylene cracker, I can tell you we do have a long-term feedstock arrangement that underpins that investment. I won't go into the specifics on that but we do indeed have an agreement there that gives us attractive feedstock economics.

And, finally, on your question on the joint venture structure. As I said, we have been very pleased with the performance of Chevron Phillips Chemical Company. They have, I think, a very strong track record in their sector and have been one of the steadily improving performers in that segment and we're happy with that.

In terms of any alternative structures, we don't comment on M&A or things like that and so I will stay consistent with our practice in not saying anything more.

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**Paul Cheng** - Barclays Capital - Analyst

Okay. A very quick one on the Upstream. Jeanette, for the under-lift in this quarter say \$115 million. It looked like the second quarter was pretty flat in terms of -- or pretty balanced and you didn't really have an over-lift or under-lift. Should we assume the entire \$115 million is a result of the third quarter, of the under-lift?

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**Jeanette Ourada** - Chevron Corporation - General Manager, IR

Paul, the bar that shows on that graph is comparing absolute liftings in the second quarter to the third quarter, so it's the value differential between those two.

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**Paul Cheng** - Barclays Capital - Analyst

Right. I --.

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**Jeanette Ourada** - Chevron Corporation - General Manager, IR

My comment about the under-lift in the quarter, so compared to production in the quarter we were under-lifted by 3% in the third quarter. I think I told you on last quarter's call in the second quarter we were about 1% over-lifted.

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**Paul Cheng** - Barclays Capital - Analyst

Okay.

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**Jeanette Ourada** - *Chevron Corporation - General Manager, IR*

So definitely a swing between quarters.

**Paul Cheng** - *Barclays Capital - Analyst*

I see. Okay, very good. Thank you.

**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Hey, Paul. This is Pat; I just wanted to go back and add one thought to the question on the joint venture structure. We have tremendous alignment between ourselves and Conoco. Usually when you have good aligned between the partners things work out really quite well and the structure doesn't become as big of an issue.

**Paul Cheng** - *Barclays Capital - Analyst*

Thank you, Pat.

**Operator**

Mark Gilman, The Benchmark Company.

**Mark Gilman** - *The Benchmark Company - Analyst*

Good morning, guys. I had a two-parter for Mike and then one Upstream question.

Mike, I was wondering if you could give me some idea as to the total cost of the Yeosu hydrocracker and what kind of return you expect there. And also address what you're likely or may be considering doing with your West Coast problem child, which I call Richmond.

On the Upstream side of the business, Pat, you might be able to respond to this. With the success that you continue to have in terms of exploration for Australia in the Northwestern Shelf, is any consideration being given to scaling up Wheatstone -- not just in terms of potential down the road expansion opportunities, but to go with a much larger project right up front similar to what happened with respect to the progression of the Gorgon project?

**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

All right. Well, I will start out. On Yeosu, it's actually a question that -- I'm not going to give you the total cost on it because actually there is some portions of the projects that are not yet completed so there is an FCC that is a second part of this to take some of the gas oil off the new vacuum column there that was started up a couple of years back so we don't have costs all in.

But I can tell you it's below budget and it's very competitive as we benchmark through IPA and the industry benchmarking processes. They have a consistent history of delivering projects at very strong capital efficiency. The other thing I will tell you is it's completely funded out of their cash flow and from their balance sheet. We don't inject any cash into GS Caltex.

Relative to your question on Richmond, we love all our children whether they are problem children or not and we are continuing to work to try to find a solution there. I think since the last time that we were together in March the California Appeals Court

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has ruled on the lower court ruling on the EIR. At the time that we were together in March we had made our appeal but we had not heard back.

They ruled in favor of the plaintiffs, which we continue to disagree with, but that is the ruling of the court. Where we are right now is in discussions with various stakeholders to see if we can find some sort of a reasonable solution here. The stakeholders include the city of Richmond, senior representatives from both the legislature and other political officials in the state in the plaintiffs on this thing.

I can't predict the outcome of the discussions. We're trying to find a reasonable solution that allows us to maintain a competitive facility in Richmond. We have been operating there for more than 100 years and we hope to continue to do so competitively, but there are some realities that we have to face as well. And so the discussions have been ongoing for some time and we're still hopeful that we will find a solution there through that path.

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

Okay. And just on the Wheatstone question, as you know, we've got project underway for capacity of about two trains of 4.3 million tons per year. So that gives you 8.6 million tons. We actually have plot space at Wheatstone for maybe five to six trains, but in addition to just having the plot space we obviously have to go after the environmental permits as well.

So I think the best answer to your question, Mark, really is that our team will be looking at what, in looking at the gas availability that we have, the plot space that we have, the economics, and then also the environmental issues, that will really -- that combination of factors will really dictate optimum expansion at Wheatstone.

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**Mark Gilman** - *The Benchmark Company - Analyst*

Okay. Thanks, guys.

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**Operator**

Faisal Khan, Citigroup.

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**Faisal Khan** - *Citi - Analyst*

Good morning. Mike, on the chemical business, I was curious, given what is going on in U.S. natural gas prices, would you guys be reinvesting to process kind of more lighter end products? I guess how do you think about that across your whole global portfolio, given where U.S. domestic natural gas prices are and the advantage feedstock you have here now?

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**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Yes, it's a great question, Faisal. I mean U.S. ethane crackers have a nice advantage right now over other U.S. feedstock alternatives and also over other European or Asian naphtha crackers. CP Chemicals U.S. assets can crack a lot of ethane. They are really geared towards a gas feedstock and they are differently advantaged in that regard versus other U.S. competitors who, as a group, have lower ability to crack ethane.

So what we see right now are the light crackers are really running full and the derivatives out of those units can compete pretty favorably in export markets. And those markets have been growing.



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So I think in the near-term we certainly see strong utilization [and] really good performance out of our existing assets. The question as to whether or not there is a long-term sustained investment case for new capacity is a different question. And I think that that is one that we need to see more evidence on the long-term sustainability and cost structure of the shale gas industry in this country and it's one that as being watched very closely.

But I would say that the near-term effects have been very positive for light crackers. The question about future investment is one that is clearly on people's minds, but I don't know that I'm ready to say anything more than that at this point.

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**Faisal Khan** - *Citi - Analyst*

Okay. And then if you are looking at your global portfolio, have you shifted more production to the US and away from other parts of the world because of this lower feedstock environment?

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**Mike Wirth** - *Chevron Corporation - EVP, Downstream and Chemicals*

Well, if you were to look at the portfolio ex the start-up and Qatar that I talked about and you see the stronger utilization in the U.S., I think the answer to that would be yes. But we do have the new capacity that is coming on in the Middle East which is a very large -- it's a 1.3 million ton per annum cracker.

And so I think net-net you wouldn't necessarily see that shift because of the impact of the new capacity in the Middle East.

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**Faisal Khan** - *Citi - Analyst*

Okay, got you. Now an Upstream question, if I can. Just give us -- repeat your comments on Jack/St. Malo? Did you say you would or would not book reserves at the end of this year?

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

We will not be booking reserves at the end of this year.

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**Faisal Khan** - *Citi - Analyst*

Okay, got you. And then what's the status of Big Foot?

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**Pat Yarrington** - *Chevron Corporation - VP & CFO*

We are still hopeful of going to FID before the end of this year.

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**Faisal Khan** - *Citi - Analyst*

Okay, great. Thank you very much.

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**Operator**

Pavel Molchanov, Raymond James.

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**Pavel Molchanov** - *Raymond James - Analyst*

Thanks for taking my question. Just one kind of conceptual, if I may. You guys have been pretty much the only company in your peer group to stay away from North American shale gas and I don't think anybody would fault you for that at all. But my question is, what would you like to see change before pulling the trigger on some of those opportunities or is that just completely off the table for the foreseeable future?

**Pat Yarrington** - *Chevron Corporation - VP & CFO*

You know, we are not opposed to shale because it's shale gas. I think we have expressed that because we have been out picking up acreage in Canada and Poland, Romania. What we have been trying to do is have a very cost effective entry point and we have not found that to be the case in the U.S. market. That is not to say that that will never be the case but we haven't found it to be the case right now.

As you know, there is a lot of spread between quality of shale properties and so it really is important the asset quality that you are acquiring.

**Pavel Molchanov** - *Raymond James - Analyst*

Absolutely. And then a quick fill up on that. In your European shale opportunities, I guess Poland in particular, what kind of timeline do you see for development into 2011 in terms of how many rigs you will allocate, etc.?

**Pat Yarrington** - *Chevron Corporation - VP & CFO*

We don't -- I don't have the full plan on this. We are just in the acquiring seismic, shooting seismic at this point in time. It's just very early days for Poland.

**Pavel Molchanov** - *Raymond James - Analyst*

Okay, very good. Thanks.

**Operator**

John Herrlin, Societe Generale.

**John Herrlin** - *Societe Generale - Analyst*

Yes, hi. Just some quick ones. With the sale of the Colonial Pipeline will you be booking a gain? And if so, how much?

**Pat Yarrington** - *Chevron Corporation - VP & CFO*

We will be booking a gain. What -- we'll indicate it when we get to it on our interim update, but certainly it will be a material item for us and we will call it out.

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**John Herrlin** - Societe Generale - Analyst

Okay, that is what I was wondering. With Jack/St. Malo I know you are not going to be booking any reserves, but regarding the development are you going to be fracking the wells before you flow them or are you going to flow them and then frack them?

**Jeanette Ourada** - Chevron Corporation - General Manager, IR

That sounds like a great question for George.

**Pat Yarrington** - Chevron Corporation - VP & CFO

We will have to get back to you on that.

**John Herrlin** - Societe Generale - Analyst

Okay, all right. Then the last one for me. You are just starting back up again in the Gulf of Mexico; things are going to go slow. The BOEM said that cost would rise for the industry about \$183 million. I know it's probably too early to assess it; I was wondering time wise whether you thought it would be kind of a 2012 event or a late 2011 event before you get a PV sense of how projects will be affected for you?

**Pat Yarrington** - Chevron Corporation - VP & CFO

Right. I mean I think we're going to have to watch this as it unfolds. What I would say is that a lot of the recommended changes in procedures and process, Chevron already had and was operating to a very high standard and already had those costs essentially as part of our way of doing business. So while there could be some incremental cost I think of it in terms -- more in terms of delay and a little bit of overhead burden than really anything more substantial than that.

When we look at our projects, of course, we take into account a variety of scenarios on commodity prices but also on cost. And our view of this cost increment that may come from the moratorium will be very small and certainly well within the bounds of the project economics that we already evaluate.

**John Herrlin** - Societe Generale - Analyst

Thank you.

**Operator**

I'm not showing any other questions in the queue at this time. I would like to turn it over to Pat Yarrington for closing comments.

**Pat Yarrington** - Chevron Corporation - VP & CFO

All right. Well, I want to thank everybody for being on the call today. We do appreciate everyone's participation and I especially want to thank the analysts who on behalf of all of the participants for their questions.

Thanks very much. Appreciate your interest in Chevron. Goodbye.

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**Operator**

Thank you. Ladies and gentlemen, this concludes Chevron's third quarter 2010 earnings conference call. You may now disconnect.

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