

OMV Petrom Q1 2020 Conference Call – Q&A Transcript

OMV Petrom published its results for January – March 2020 on April 29, 2020. The investor and analyst conference call was broadcast as a live audio-webcast at 3:15 pm local time. Below is the transcript of the question and answer session, by topic, edited for readability.

Group

1. Balance sheet

Question from Alexander Burgansky (Renaissance Capital): I have a question on your balance sheet. We have seen an increase in other financial assets on the balance sheet. So can you please explain or remind us what these other financial assets relate to? And also, I notice that you did not include this one in your net debt estimates. So can you please elaborate as to why this is not included in net debt?

Answer from Alina Popa (CFO): Our other financial assets are increasing and the same you might see on the financial liabilities side. What we have reflected there are the margin hedges, the fair valuation of the margin hedges, which is done on a monthly and quarterly basis. So if you look into our investor news, we have a note with a little bit more disclosure around financial assets and financial liabilities. And you will see a net value of these margin hedges around RON 300 million. That is the item and we do apply hedge accounting for that.

They are not included in the net debt. So the net debt definition is simply cash minus debt plus or minus leasing. You might notice that now we added two definitions – one with leasing, one without leasing – but definitely financial assets representing these hedges are not included in the net debt definition.

2. Sensitivity to oil prices - impairments

Question from Cristian Petre (NN): Just one quick clarification. So your long-term oil price now is \$75, right? So, if the potential impairment, if you adjust the long-term oil price to \$60, it will be between RON 1.2 and RON 1.5 billion.

Answer from Alina Popa: So what we have done, maybe just a clarification – this is an important topic. We have revised for impairment purposes our oil prices for 2020 and 2021 going from \$60 to \$40 in 2020 and from \$70 to \$50 in 2021. As a result of that, we have booked impairments now in Q1. Of course, we are considering and looking on the mid- and long-term oil price assumptions and in our latest impairment test, we had around a \$75 long-term oil price assumption. Now, we have not yet decided how we see long-term oil price assumptions, particularly for sensitivity, and this shows that if it is \$60 long term, then we will have impairment of this size, RON 1.2 to RON 1.5 billion. And this will be decided to be booked in the next quarter of this year, exactly.

Question from Cristian Petre: And what was the impairment in quarter one?

Answer from Alina Popa: € 6 million, RON 28 million.

Downstream Oil

3. Refining segment: utilization rate, margin hedges and CO2 certificates sale

Question from Oleg Galbur (Raiffeisen): I will start with the refining segment. And the first question or rather group of questions refer to the Downstream Oil which had an outstanding performance in the first quarter and I wanted to ask you to help us understand what was driving such a strong generation in the quarter, whether those are rather one-time factors or more sustainable developments which could be replicated in the quarters?

Answer from Alina Popa: Downstream Oil showed a strong performance in Q1 and this was helped definitely by the improved refining margin and also, a good situation on the demand side as the impact of coronavirus was only felt towards the end of March.

We also mentioned the effect coming from margin hedges, approximately RON 60 million coming from margin hedges. And I would like to mention a one-off which was the sale of CO2 certificates. So we had CO2 certificates coming from the past belonging to Downstream Oil which have been sold in Q1. And out of this sale, we had a one-off impact, approximately RON 160 million shown in the Downstream Oil. So this is a one-off effect which we should not consider for the future quarters.

To mention also that at group level, part of these CO2 certificates have been reversed in the consolidation. So the impact at group level is lower. It is around RON 40 million coming from the sale of CO2 certificates. So that is with regard to the refinery impact.

What we see for 2020 is an utilization of around 85% for the year. Previously, forecast was about 90% so now we go to 85% for 2020 and for Q2 around 80%.

Question from Raphaël Dubois (Société Générale): on the CO2 certificates, can you just explain what is it exactly that you are selling? Is this because of you revising down your level of activity going forward, i.e., you need less CO2 or is this gambling that CO2 prices will fall further?

Answer from Alina Popa: We had CO2 certificates coming from the past, which were not needed for this year. So looking at the market, our experts suggested that the CO2 price would go further down. That is why we decided it is better to realize this and we sold the CO2 this year. As I mentioned, we did not need them for this year. So for the following years, we will purchase what would be needed. So that was the context into the CO2. That is why it was purely an one-off impact.

Question from Oleg Galbur: And what level of utilization have you planned for the second and third quarter of this year?

Answer from Christina Verchere (CEO): The one other thing I would just add to the utilization on the refinery side is that we have moved our shutdown into July. So again, that helps us with the utilization and managing the supply-demand situation both in the second and third quarter, which is why we believe that we can manage the utilization.

The other aspect to add is that given that we are at the 80% - 85% level, the majority of this is our equity crude that is going through the refinery so less on imported crude being bought for the refinery side.

Question from Tamas Pletser (Erste Bank): I just wonder if you face a further decline in the demand, would you keep the refinery utilization rate of 80% - 85% in order to process your equity crude or would you look for any other solutions like reducing the refinery utilization further down and storing the oil or keeping the utilization and start trying to export the products you produce? So what will be your reaction to the further decline of the demand especially if your competitor, Petromidia, would come back to the market?

Answer from Christina Verchere: I think the question is how much flexibility do we have in our current estimates should we see a further drop in demand? First of all, we will optimize all of our storage capacity that we have both of crude as well as the products and we have a fair amount of storage capability around the country.

Other aspect of that is we are actually able to get products to the coast and find export routes as well from the country. So we are not a land-locked refinery. We feel that there are enough options. And then obviously, we will be able to adjust some of the utilization accordingly.

In the end, any decisions with regard to shelving in production or anything like that will be economically, regulatory, and legally driven decisions. That will take into account the full integration of our business. At this point in time, we believe we have the flexibility to be able to manage this situation.

Question from Raphaël Dubois: Could you please tell us if you see any signs of Rompetrol refinery getting ready for start-up after its turnaround? And one more question, you have adjusted downward your refinery runs. Why do you not also adjust your upstream production down then?

Answer from Christina Verchere: With regard to Rompetrol, probably not best for us to comment on another operator but be assured, we are aware of the different refinery runs that are going on in Romania and have taken them into consideration with regards to our expectations going forward on that.

With regard to the refinery, while we believe that we can take the refinery runs down and not take upstream production, it is fundamentally that actually generally when a refinery is running at sort of its highest level of utilization, which is generally around the 95% to 98%, actually about 80% to 85% of that is equity crude. So now that we have taken it down, actually we are able to maintain the upstream equity production because that is the flow that refinery is running at now. So obviously, we are optimizing our storage, as you can imagine, as we look at the second quarter. We have a shutdown as well. So we are optimizing and making sure we do that. But at this point in time, we are able to maintain all of our upstream production, ultimately because the refinery has allowed the capacity in our production.

4. Demand for fuels

Question from Oleg Galbur: Also here, if you could share with us how the motor fuel consumption in Romania currently does look like during the lockdown, by key products if possible?

Answer from Christina Verchere: On the demand side, what we are forecasting for the full year is a decrease in sales of about 15% to 20% for the full year, with the strongest impact being in the second quarter, with a slightly higher impact on gasoline versus diesel. We did not talk too much about jet, but just to highlight that jet only makes up for about 3% of our yield from the refinery. So it was not so exposed to the jet implication with the aviation side of it.

Upstream

5. Capex decline and impact on production

Question from Oleg Galbur: I would like to ask you to help us assess the impact of Upstream CAPEX reduction this year on the next year's oil and gas production. Provided that crude oil improves towards the end of the year or next year, would Petrom be able to quickly offset the impact of lower CAPEX this year or should we assume a more abrupt production decline over the next two years?

Answer from Christina Verchere: Regarding Upstream CAPEX and next year's production, we are not yet ready or able to provide an implication for next year. I think the one thing that we would say about our portfolio is that we can actually flex. We can flex quite a lot in the portfolio. There are some pluses to that, it means that we can ramp your CAPEX relatively quickly and see the production side, because we can tie in well relatively fast. Likewise, it flips the other side when you reduce the CAPEX down. But the other aspect is that a lot of our volume is on our workovers and actually, we are maintaining that activity throughout 2020 at this point. Again, we will need to be flexible should conditions change differently than we expect.

6. Opex/boe

Question from Raphaël Dubois: Just one question on your OPEX per BOE. I see that it has come down year-on-year but quarter-on-quarter; it is up despite a very resilient production level and foreign exchange going your way. So can you maybe just explain what happened quarter-on-quarter?

Answer from Christina Verchere: On the OPEX, Raphaël, let us get back to you on the quarterly trends. I think what I would say is that overall, yes, we had a stronger quarter of production in the first quarter. We do see some different trends quarter-by-quarter with regards to OPEX overall. But we will come back to you on details.

Downstream Gas

7. Gas market: demand, regulations

Question from Question from Irina Railean (Banca Transilvania): I would like to ask a question about the gas market outlook. How do you assess current market conditions? How do you expect the market to be impacted by the coronavirus? Is the demand expected to decline as much as fuel? What is your view on this topic?

Answer from Christina Verchere: Regarding gas production, similar to oil production, it has not been impacted in any way by COVID and by the change in demand levels. We are still able to get our product to customers. When we look at the trend for demand and our estimates for it, we see in the low double digits, a low double-digit drop versus prior year. So we do see a decrease overall. However, Romania is a net importing country so we would anticipate seeing that as predominantly being a reduction in imports.

Question from Tamas Pletser: It is not really clear for me whether based on the current regulatory framework, can we expect a full liberalization of the gas market from the middle of the year? How do you understand the current situation because, as far as I know, this has not been clarified yet with how the regulatory framework would look like from the middle of the year?

Answer from Christina Verchere: As a reminder, GEO 1/2020 restated that we would see a liberalized market in gas from 1 July 2020 and for electricity from 1 January 2020. ANRE has issued for public consultation the regulations that would fit under that and we are in dialogues through the association on that.

One thing that we are looking for is we are keen to see a gas release program put in place instead of the central market obligation. We believe, along with others and amongst the association, that this will provide a better market signal for the gas price in Romania and it will improve visibility.

No final decision has been made yet and it would require legislative changes. Therefore, I hope that when we talk to you again in one quarter's time, we will be able to see a full set of answers for you. However, consultation is underway with the regulator.

Question from Tamas Pletser: So you say basically that the concrete law has not been in place, has not been approved yet, which basically liberalizes the market.

Answer from Christina Verchere: The law is there to liberalize the market. What we still see is a central market obligation and we believe that there is a better mechanism than the central market obligation. So we would like to see a gas release program. To get a gas release program and remove the central market obligation requires legislative changes.

I will say that the efficiency of the liberalized gas market and how the market works is what we are trying to see improvement in.

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