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EDITED TRANSCRIPT

COP - Q4 2015 ConocoPhillips Earnings Call

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OVERVIEW:

Co. reported 2015 adjusted net loss of $1.7b or $1.40 per share and 4Q15 adjusted net loss of $1.1b or $0.90 a share.

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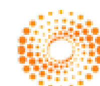

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PRESENTATION

Operator

Welcome to the fourth-quarter 2015 ConocoPhillips earnings conference call. My name is Christine and I will be your operator for today's call.

(Operator Instructions)

Please note that this conference is being recorded. I will now turn the call over to Ellen DeSanctis, VP, Investor Relations and Communications, ConocoPhillips. You may begin.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Christine, and good morning to everybody. Today you will hear from Ryan Lance, our Chairman and CEO, Jeff Sheets, our EVP of Finance and Chief Financial Officer, and Matt Fox, our EVP of Exploration and Production. We will be making some forward-looking statements this morning and our cautionary language is shown on page 2.

That information can also be found in our periodic filings with the SEC. We do anticipate a lot of questions today, so we'll limit our questions to one and a follow-up when we get to Q&A.

And now I'm going to turn the call over to Ryan Lance.

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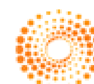

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Ryan Lance - *ConocoPhillips - Chairman and CEO*

Thank you, Ellen.

I'm going to let Jeff handle the 2015 recap in his upcoming comments and I'm going to jump right into the news we announced today beginning with slide 4. With today's announcement regarding reductions in our operating plan and our dividend, we have taken significant actions to reset the company in response to much lower commodity prices and tightening credit markets across the industry.

These are two factors that have changed significantly in our view in a short period of time. And they have important implications for the sector, especially in 2016 and 2017. Regarding prices, there are three factors that are driving our actions. First, current prices are much lower than we expected at the time we announced our 2016 operating plan. This is amid bearish supply/demand signals and record levels of inventories. Brent is currently trading 40% lower than 2015 average prices.

Second, we believe this downturn could last a while longer. Just a few months ago, we thought the market would rebalance by the second half of 2016. Now it looks like that could stretch into 2017. And third, greater concerns about global growth suggest it could take longer to reach an equilibrium mid-cycle price after balancing occurs. Now certainly there's a lot of debate about these factors, but we can't bet on prices turning quickly.

Instead, we're taking what we believe are prudent actions to prepare for a weaker price environment and for a longer period of time. Regarding the credit markets, it's no secret that the credit rating agencies also see a likelihood of a weaker, more protracted downturn. Recently Moody's and S&P have issued significantly lower price decks. The agencies have industry under review for credit rating downgrades.

Moody's has stated that multi-notch rating downgrades are likely and some have already occurred. The consequences of these downgrades are that debt capacity will shrink across the sector. For ConocoPhillips the bottom line is this; we're going to take actions to maintain a strong balance sheet. We believe this is critical and will be a key differentiator in this business.

So as difficult as these choices are, and they were very difficult, we must do the right thing for the company. As we announced, we're taking two key actions to respond to these factors. First, we are further reducing our 2016 operating plan capital and operating expense. Now for the past 18 months, we've lowered capex and opex levels across the company as prices have weakened, and we're doing it again in 2016 and that's shown on slide 5.

This slide summarizes our revised 2016 operating plan. It represents a significant shift compared to last year and an even bigger shift compared to 2014. Now importantly, these reductions we're making will improve net cash flow in 2016 by $2 billion compared to the plan we laid out in December. On the left side of this chart, you can see we're lowering our 2016 capital expenditures to $6.4 billion.

That's a reduction of $3.7 billion compared to 2015 and $1.3 billion compared to our original 2016 operating plan. We're dropping down to three rigs in the Lower 48 because it doesn't make economic sense to maintain our original level of activity at current prices. And we don't lose acreage or optionality.

We're cutting other discretionary programs across the business, which are somewhat offset by anticipated cash calls in our equity affiliates. Our original plan anticipated 1% to 3% production growth in 2016. Now we expect flat production given these capital cuts. We're letting Lower 48 volumes decline, but these will be offset in the near term from ramp up at APLNG and in the oil sands.

Finally, we continue to improve our operating costs. We set an initial budget of $7.7 billion for 2016. We're now lowering that to $7 billion. But we don't believe these reductions are sufficient to maintain our strong balance sheet under the lower for longer circumstances I just described. And so we've taken a second and more difficult step of reducing the dividend.

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This morning we announced reducing the quarterly dividend to $0.25 per share effective with the first-quarter 2016 dividend payment. And this is discussed on slide 6. In mid-December, we reaffirmed that our dividend is the top priority use of cash. In 2016, this was premised on using up to a couple billion dollars of balance sheet capacity based on similar prices to 2015.

After making those adjustments to our operating plan that I just reviewed, we analyzed the impact to our balance sheet under conditions where prices stay in the $30s for longer. We came to the conclusion that our balance sheet could get stretched beyond a prudent level. Ultimately, we believe we needed to make a tough choice between protecting the current level of the dividend or maintaining our strong balance sheet through an extended downturn.

We made a decision to reduce the dividend. This action, combined with the operating plan reductions, will improve net cash flow by about $4.4 billion in 2016. Once we made that decision, our primary consideration was to set a dividend that will be sustainable through the cycles. We are balancing several objectives, including yield, financial strength, and lowering the breakeven cost of our business.

We set the dividend at a level that we believe results in a competitive yield. The dividend will continue to be a top priority. It provides important discipline on our investment programs and will remain a core part of our offering. We believe our dividend is at a level that preserves balance sheet strength and provides financial flexibility through the current downturn. These actions also lower our breakeven price to roughly $45 per barrel Brent.

And what we mean here is that we can keep production flat and pay our dividend for many years at $45 per barrel without needing to sell assets or increase our debt levels. This significant improvement in our breakeven price will allow us to generate greater profitability and cash flow growth when the cycle turns. And the combined reset of capital, operating costs, and the dividend will enable us to generate free cash flow that we can deploy across a range of choices, including increased investment into our low costs of supply resource base, but also including returning capital to shareholders.

The reset will allow us to grow our dividend in the future as our cash flows grow and at a much lower mid-cycle price. That goes without saying that these were very difficult actions to take. But they will improve our ability to manage through the price weakness the industry is facing.

They will improve our medium-term outlook by allowing us to accelerate performance as prices turn, and they will help the long-term performance of the business by making us more resilient in a world of lower, more volatile prices.

So now let me turn it over to Jeff and Matt, and I'll come back at the end to conclude my remarks.

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Thanks, Ryan.

I'll begin my remarks on slide 8. And as Ryan said, I will open with some brief comments about 2015, the summary of which are shown on this page. Measured against the standards of delivering the things within our control, it was a strong year. Strategically, we lowered our capital expenditures by more than 40% compared to 2014.

We achieved $2.2 billion in disposition proceeds from the sale of non-core assets, primarily North American gas assets. And announced our intention to begin a phased exit of deepwater exploration. Operationally, we achieved 5% year-over-year production growth, excluding Libya and downtime and dispositions. That exceeded our initial guidance for the year and came mostly from the development drilling programs and the ramp up of production from our major projects.

We also achieved first production from Surmont 2 and first LNG from APLNG, which were big milestones for the company. Financially, we had an adjusted net loss of $1.7 billion or $1.40 per share. This includes a fourth-quarter adjusted net loss of $1.1 billion or $0.90 a share. We recognize that analyst consensus was negative $0.64 per share and we believe this difference primarily reflects the $506 million of dry hole expense in the

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quarter in our adjusted earnings, which we think is about $0.15 higher than consensus estimates. The FX impacts account for the balance of this difference.

Finally, we had $7.6 billion in cash flow from operations, excluding working capital, and ended the year with $2.4 billion of cash on the balance sheet. I'll now walk through our cash flow waterfall on slide 9. On this chart, you can see the major buckets of cash sources and uses for the year. We started the year with $5.1 billion in cash and generated $7.6 billion from operating activities, excluding working capital. Working capital was about a $1 billion use of cash during the year.

We captured about $2.2 billion of net proceeds from dispositions and took on about $2.4 billion of debt. Our 2015 capital expenditures were $10.1 billion. And after accounting for dividends and some other items, we ended the year with $2.4 billion in cash.

Turning to slide 10, I'll cover some thoughts on the balance sheet. A period of low prices highlights the importance of a strong balance sheet in this cyclical business. However, a consequence of the recent price drops has been that the credit rating agencies have become very pessimistic about future prices and they are currently reviewing the industry's credit ratings using much lower forecasted prices.

We should see industry-wide credit downgrades over the next couple of months with the potential for multi-notch downgrades in some cases. Across the industry, this is going to result in reduced debt capacity within given rating bands, compared to just a few months ago. We believe the reduction in the dividend, and the substantially lower risk of significant borrowings as a result of that decision, will help mitigate the credit rating impacts.

We are well positioned should we need to acquire additional debt capital. We ended 2015 with over $8 billion in liquidity, comprised of $2.4 billion in cash and about $6 billion of available debt capacity on our revolving credit facilities. We expect to see significant levels of borrowings among our peer companies this year and our liquidity balance will give us the flexibility to access the capital markets at the time of our choosing and avoid a very crowded energy market for energy sector debt this year.

In terms of how much debt we will need to raise in 2016, our current estimate is that we will utilize our cash balances and not need significant additional debt if oil prices average around $40 for the year. By making the difficult decision to reduce our dividend, we believe we are positioned to preserve a strong balance sheet in a prolonged period of low prices such as the ones we're seeing today.

While we have been successful over the last several years in selling assets at full value, during a period of higher prices and strong demands for assets, another important benefit of making the changes we announced this morning and maintaining balance sheet capacity is that asset sales are not necessary to bridge funding gaps. That concludes my comments. Note that our appendix includes some updated net income sensitivities and some additional 2016 guidance items.

Now I will turn the call over to Matt for his operational comments.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Thanks, Jeff.

I'll review our operational performance beginning with our 2015 reserves. Final reserve details will be published in our 10-K in late February, but we don't expect these numbers to change significantly. On slide 12, you will see that we started the year with 8.9 billion barrels of reserve. We produced 610 million barrels and had additions of 523 million excluding market factors. So on that basis, our adjusted replacement ratio was 86%.

However, because our portfolio is dominated by tax and royalty regimes, there was significant price-related reserve impacts in 2015. The lower price effect reduced our year-end reserves by 353 million BOE. In addition, also due to lower prices, we've reduced our expected capital program for the next several years. This slower pace of development has resulted in a booked reserve reduction of 111 million BOE.

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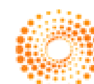

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Now these combined 464 million barrels have not gone away because prices have dropped. So we expect to rebook reserves as prices improve. Adjusting our additions for the price effect and the planned capital reductions, we had organic reserve additions of 59 million barrels, which results in an organic reserve replacement ratio of 10% of 2015 production. Reserves were further reduced by 175 million BOE, primarily as a result of non-core asset dispositions. So our total reserve replacement ratio, including both dispositions and market factors, was negative 19%. As I said more details will be available in our 10-K filing.

Now I'll cover our operational priorities for the year on the next slide. The midpoint of our 2016 production range is expected to be essentially flat to 2015 production when you adjust out the full-year effects of asset sales. In the first quarter, production is expected to be between 1,540 thousand and 1,580 thousand BOE per day.

Production will be lower in the second and third quarters as we see our usual downtime from major turnarounds. And then in the fourth quarter, as we move out of turnaround season, we'll see increased production associated with major project ramps at places like Surmont 2 and APLNG and the production associated with development activity across the globe.

In Alaska, we're still progressing our GMT1 project and a winter exploration program around existing infrastructure. In the Lower 48, we'll be focused on assessing the results of multiple pilot tests we conducted in 2015. This will allow us to optimize development plans as we prepare for a future ramp up as our price outlook improves.

We also expect to complete our Gulf of Mexico exploration programs before year end. In Canada, ramp up continues at Surmont 2 and we have 2 exploration wells being drilled offshore Nova Scotia. In our Europe and North Africa segment, we will continue development drilling in the Greater Ekofisk Area and we expect first production from Alder in the second half of the year.

At APLNG, we're now shipping LNG from Train 1. We've shipped four cargoes already and the plant is running well. We also expect the startup of Train 2 in the second half of the year. Finally, in Other International, the second well on our offshore Senegal SNE discovery had very encouraging test rates. We've just finished drilling the third well and are currently preparing to test.

It looks like 2016 may be an even more challenging year for the industry than we experienced in 2015. But we remain focused on what we can control, delivering best-in-class operational and safety performance, and we're ready to ramp up the development of our diverse, flexible, low cost of supply resource base when prices recover.

Now I'll turn the call back to Ryan to wrap up.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Thank you, Matt.

Certainly the journey through this price downturn has been a test for everyone in this industry. The easy moves were made a long time ago. Today we announced one of the toughest decisions. But we believe it's the right decision given the circumstances facing the industry at this time.

We can't count on a quick fix for prices, and we're not willing to risk a strong balance sheet on it. These actions will result in immediate benefit to our cash position, create the necessary flexibility to endure a longer downturn, and put the company in a better position for a strong performance as prices recover. So thank you.

And we'll turn it back over to the operator for questions.

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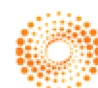

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QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

Our first question is from Ryan Todd of Deutsche Bank. Please go ahead.

Ryan Todd - *Deutsche Bank - Analyst*

Great. Thanks. Good morning, everybody. Maybe if I could just start with can you talk a little bit more about, I know you highlighted some of it in the presentation, but what changed in the last eight weeks? What were the primary changes that convinced you, one, that we were going to be lower for longer, and does this involve a material change in your view on the mid-cycle price as well? What were the primary changes behind first priority and cash capex to a cut?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes, Ryan, it was a difficult decision. What drove that is what we talked about in our prepared remarks a bit. You know, the world has changed, and it's been a dramatic drop in prices. So we're seeing and enduring a much lower drop in prices and as we look at the fundamentals, it looks like balancing probably is shifting until later in 2016 and possibly moving into 2017.

So really it was the depth of the drop over the last eight weeks to two months, combined with the duration. And the inventory doesn't seem to be flattening, let alone starting to drop off. And that combined with the last month of conversations that we've been having with the rating agencies. And clearly the debt capacity is going to be reduced. So when we came out with our operating plan in December, we talked about using the balance sheet to get through the cycle.

And now the capacity is reduced, the cycle has deepened and potentially gotten longer. So we have to prepare for that. And we made the difficult decision of preserving the balance sheet over the dividend at that time.

You asked about mid-cycle price. That's a tough one. It looks like it's going to be longer to get there and there's some downsides and some up sides to that conversation.

The downside is supply has certainly been more resilient than most people expected, and we're still building inventory. Certainly OPEC for now is protecting price, or not protecting price, and doing that, so they're protecting market share. I think we've seen the resiliency in the unconventional revolution.

It's opened up a new supply source that is more flexible, lower cost of supply than some of the other conventional productions like deepwater. And certainly some concerns about economic growth. So those are the kind of the things for the downside that would suggest a lower mid-cycle price. But there's other factors. Certainly the capital cuts that the industry is making should result in a supply rebound. Or supply shock to the downside.

And certainly the Saudis could lead OPEC to a different decision whenever they feel like the point they're trying to make has been made, and certainly the lower prices are stimulating demand. So there's pieces on both sides of this thing that balance out the concern about where mid-cycles might be going to. In the past, we've had a view of mid-cycle prices in the mid-$70s, but we're currently taking a look at that.

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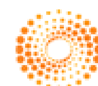

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Ryan Todd - *Deutsche Bank - Analyst*

Great. Thanks.

And then maybe, I guess as we look beyond 2016, how should we think about your effort to balance cash inputs and outputs? Will you seek to ramp spend in line with cash flow, but covering cash flow and dividend in line with changes in cash flow, and is the first call on any sensitivity around that, is that plus or minus on the Lower 48?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes, we'll manage the free cash flow. We'll set a capex budget and the dividend level to manage to make sure we can manage as prices come back. Any free cash flow that we have at that point in time, we can send back, as I said, we can send back to shareholders, or we can put that back into our deep inventory of low cost of supply capital investment options.

So that's, granted, a very difficult decision that we made, but part of that is setting a lower breakeven cost for the company. And we're convinced in a world of lower, we can debate what the mid-cycle price is going to be. It's going to be more volatile. And we're going to create flexibility to have free cash flow as the prices recover and be able to react to the volatility we think the market is going to have.

Ryan Todd - *Deutsche Bank - Analyst*

Thanks. I appreciate it.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Ryan.

Operator

Thank you. Our next question is from Doug Terreson of Evercore ISI. Please go ahead.

Doug Terreson - *Evercore ISI - Analyst*

Hi, everybody.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Hi, Doug.

Doug Terreson - *Evercore ISI - Analyst*

So my question is on the business model and the value proposition, and specifically for most of the past couple of decades, this company offered lower growth to some degree, but healthy shareholder distributions through share repurchases and a reliable and growing dividend.

However, because shareholders are not really offered any of those attributes today, and I realize that we could be near the trough of the cycle and this could change, my question is how you would describe your new value proposition, and also the business model by which you plan to achieve it in the future, Ryan. So there's two questions there.

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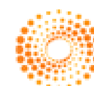

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Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes. Thank you, Doug. Appreciate the questions.

I think we're spending some time thinking about the value proposition as we go forward. I think fundamentally, at the core of that value proposition, it hasn't changed. We're committed to providing a competitive dividend. We'll have disciplined growth. We've got a deep inventory of growth options.

If the free cash flow is there to generate it, and we believe in financial strength, which is why we need to keep a very strong balance sheet. We're hitting the reset button here a little bit. And I can understand that. And it was a gut wrenching decision for us to go do that.

But fundamentally I don't think that value proposition has changed. We're going to lower the breakeven cost for the company. We'll still provide a competitive dividend and growing, as our cash flows grow. And I think fundamentally, we've still -- the low cost of supply resource base that we have in the company hasn't gone away with this change. It's still there and it still offers a lot of investment choices for the company.

Doug Terreson - *Evercore ISI - Analyst*

Okay. And Ryan, I know it may be too early to ask this question, but my follow-up is, how does the model that you guys are thinking about today differentiate itself in relation to some of these larger cap E&P companies? And the reason that I ask is because they've produced pretty dismal returns for shareholders during the past couple of decades, even with oil prices two or three times higher than they are today.

And I know that you don't aspire to that outcome, and it may not be a fair question, because it's still early and you just cut the dividend today, but what's the differentiating feature here?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Well, I think for us, too, I think we have to look at the portfolio. We'll be able to supply growth that we say could be modest, but we'll still grow. We'll have financial flexibility. We'll have a strong balance sheet. We'll generate free cash flow at a much lower mid-cycle price. And we think the world that we're going into is going to be more volatile and probably drive to a lower mid-cycle price as we go forward.

So that's the basic value proposition when we spun the company. We recognize that we may be moving down a bit on the competitive dividend that we've been offering in the past. But we think we're making up for that in some of the free cash flow and the choices then we'll have as we lower the breakeven price for the company to reinvest that into the company and/or return that to shareholders.

Doug Terreson - *Evercore ISI - Analyst*

I see. Okay, thanks a lot.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Thanks, Doug.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thank you, Doug.

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Operator

Thank you. Our next question is from Doug Leggate of Bank of America. Please go ahead.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Thanks. Good morning, everyone.

Ryan, I would like to follow on from Doug's question, if I may, because at 1.6 million, 1.5 million barrels a day, any meaningful growth without committing to another round of large-scale projects is going to be tough. So in order to be competitive with your peers.

So I really want to try and understand, you talked about the compelling dividend, not the competitive dividend in the past as making your value proposition unique. So what makes ConocoPhillips unique today? I'm thinking specifically about how you -- what your first call on cash would be in the event of any recovery. And I've got a follow-up, please.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Well, again, Doug, thank you for the question. I think at the risk of repeating myself here a little bit, I think it's -- we'll differentiate ourselves because of the low cost of supply deep resource base that we have captured in the company today, and the exploitation of it. It's flexible, it's a shorter cycle time. It will be much more predictable and it will generate free cash flow at a much, much lower breakeven price for the company. So we'll have choices.

We'll have choices to make as we go forward and the recovery occurs and prices start to come back, which we believe that will happen. And we can -- we'll have choice around how we do that, what kind of growth we think we want to generate, because we know we have the portfolio to go do that. Now, we're not talking about high single and double-digit growth rates.

That's not what we're talking about with our company. But we have a more predictable low cost of supply flexible resource base that we can invest in. And when we generate free cash flow we can decide what to go do with it. And we're committed to the dividend. It's still a priority first use of cash and growing that as our cash flows grow.

Doug Leggate - *BofA Merrill Lynch - Analyst*

On a per-share basis or on an absolute basis?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Both.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Okay. My follow-up is on the capital program. So this year, frankly I'm a little surprised that you didn't cut more, given the challenging economics across the portfolio. So I'm trying to understand what the constraints are as to why you didn't cut more.

And I'm thinking about long-life assets and how those roll off as you go into 2017. I know it's very early to talk about 2017 capital, but you've got, what, $600 million on APLNG this year and $800 million on exploration. So what are the constraints in capital? Where do you think that goes next? And I'll leave it there. Thanks.

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Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Hello, Doug, this is Matt. I'll take that question.

Of the $6.4 billion, we have about $1 billion going to maintenance capital, and we're never going to cut back on the integrity of our assets. In major projects, there's about $2 billion. And these are major projects that are well into the execution phase. As you said, there's about $700 million or $800 million going into APLNG, for example, to finish Train 2.

There's about $300 million going into Clair Ridge to better move that towards completion, and about the same going into Malikai in Malaysia. So these are project that are getting very close to their completion. We've got development capital program of just over $2 billion, $2.2 billion. And despite the cuts that we're doing in the Lower 48, there's still the $800 million of that going into North America as we ramp down our rig program.

And then we have, as you mentioned, an exploration program going on that has quite a significant deepwater component this year as we finish our deepwater program. That's a total of $1.2 billion. So we're going to be looking to execute all of that at lower costs, execute all that scope at lower costs, but currently our expectation is that'll be $6.4 billion, and that cutting any further would not be prudent, would not be in the best long-term interest of value creation for the shareholders. So that's why we stopped cutting capital at the $6.4 billion level.

Doug Leggate - *BofA Merrill Lynch - Analyst*

I don't want to hog the call here, Matt, but I want to be clear. How much of that rolls off when these major capital projects are finished is what I'm really trying to get at? In other words, where does it -- this year there seemed to be some constraints. As you say, you've got to finish what you started. What happens beyond 2016?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

As we move into 2017, we see a couple of things changing. First of all, our deepwater exploration program will be complete. That represents about $800 million this year. And we should be down to virtually zero by the time we get to 2017. APLNG Train 2 will be complete.

And in addition to completing APLNG Train 2, we actually, in this lower price environment, are also having to make contributions into APLNG and FCCL. So if you look at the total of those contributions to the equity affiliates and deepwater, that represents about $2 billion of the $6.4 billion this year. And so that's an indication of how much will be rolling off as we move into 2017.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Got it. Thanks very much.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Doug.

Operator

Thank you. Our next question is from Scott Hanold of RBC Capital Markets. Please go ahead.

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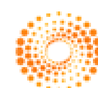

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Scott Hanold - *RBC Capital Markets - Analyst*

Yes, thanks. Could I ask a question on moving to the three rigs in the US? I think you were at, what, 13, moving to three. The trajectory in the US would likely be down, but much of that being offset, obviously, by the major project starts. What does your ability to keep production flat in 2017 look like? Where do those new sources of contribution to maintain that say in 2017 and 2018 and beyond?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

As we move from 2016 to 2017, our base decline is about 8%. So that's about 120,000 barrels a day. So we have to deliver 120,000 barrels a day of new production to stay flat. And that's going to be split roughly evenly between our development drilling programs around the world. So places like Alaska, Europe, China, and some in the Lower 48. We will still be running some rigs, and some in Canada.

And the other half is going to come from major project, completing the ramp up of APLNG, bringing the KBB project onto production, finishing ramping up Surmont 2 and the FCCL projects. So it comes from a mixture of about half and half from development programs around the world and major projects.

Scott Hanold - *RBC Capital Markets - Analyst*

Okay, then specifically, that rig count that you all referred to, do you see that materially changing as you roll into 2017 and 2018 at this point in time in order to maintain production flat?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

We would anticipate putting more rigs back to work in the Lower 48 as we move into 2017. But that's a function of the capital and that level that we decide to spend.

Scott Hanold - *RBC Capital Markets - Analyst*

Okay. And as my follow-up, when you look at, obviously, the big cuts you made to both capex and the dividend, can you discuss a little bit on how you came to the math on we needed to see a two-thirds cut here and we need to get down to $6.4 billion? Was it predicated on a certain price outlook, or how did that discussion occur?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes, Scott. I'll take that. I think it really trying to triangulate on three different issues that we have in front of us. And that is, one, we wanted to continue to maintain a strong balance sheet and minimize the borrowing in 2016, which would lead you in one direction. We certainly had what long-term break-even price do we think is appropriate and provides for a good value proposition going forward. So that factored into it.

Then certainly a desire to keep a competitive dividend, as measured by yield or other factors. So it was really a triangulation of all those things. And then factoring into that is our capital program and the commitments that Matt talked about and the capital spend that we need to have that we think makes sense for the long-term value of the company. So there were those pieces that put us in that box trying to decide and triangulate a bit on what the right level of dividend going forward should be for the company.

Scott Hanold - *RBC Capital Markets - Analyst*

Okay. Thank you.

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Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thank you.

Operator

Thank you. Our next question is from Evan Calio of Morgan Stanley. Please go ahead.

Evan Calio - *Morgan Stanley - Analyst*

Good afternoon.

I just wanted to follow up on the choices that you mentioned earlier. What's your target leverage through the cycle? I'm just trying to quantify the choice to deleverage exiting the cycle, which I presume would be a higher priority.

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Yes, I'll take that one, Evan. I think whether it's target leverage or target credit rating, and particularly on the credit rating side, it'd hard to answer any kind of thought about a target credit rating agencies because the rating agencies are going through quite a change in how they assess the industry, and we don't know really right now what debt levels are going to correlate to what credit ratings. But I think the direction of your question is right.

It's just how do we think about the level of our debt going forward. Just some general comments about debt. If you think about what we've done over the last several years, we ended 2015 with $24.9 billion, so essential $25 billion worth of debt. And three years ago at 2012, we had $22 billion worth of debt. So unlike some of the peers, in our company, we've not really added a significant amount of debt in the last several years.

And really what we've been doing as we've been an independent E&P is we've funded our capital program and our dividends mostly from cash from operations and selling non-core assets and then we've quickly made adjustments to our capital program and our operating cost structure as the circumstances have changed to try to limit our debt borrowings. But that's history.

Going forward, how do we think about the question of the right level of debt and what makes sense at different mid-cycle prices? So last year we generated $7.5 billion in cash flow in what was a $50-ish price environment. 2014, the year before that, we generated $16 billion in cash flow in what was a $90 price environment. And you could think that mid-cycle prices are going to be somewhere in that range, between $50 and $90.

We can look at $25 billion of debt, though, and feel like that's a reasonable amount of debt to have in either of those mid-cycle scenarios. So consequently, as prices improve, we don't feel like we're going to be compelled to use cash flows to reduce debt levels. So delevering is not going to be a priority for us.

Evan Calio - *Morgan Stanley - Analyst*

Okay. Thank you.

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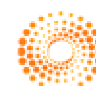

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Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

But we're not comfortable, and this is what you've heard from us today, is we're not comfortable with having a plan that relies on the heavy use of debt financing to fund cash shortfalls in a period of really low prices. And that's where we felt like we were going to be if we continued the current dividend, and we'd be rapidly using balance sheet capacity while we were waiting on some commodity price improvement.

Evan Calio - *Morgan Stanley - Analyst*

Great. My second question, you mentioned no asset sales are needed to bridge the funding gap under your book commodity assumptions. Is that a conservative view, or does that reflect your view that fair prices may or do not exist in the current environment? Any update there on your current process and if that statement means anything about that current process.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Well, no, we've said in the past, portfolio of our size, to expect $1 billion to $2 billion of asset sales. We just don't think relying on a significant number of asset sales to bridge a cash flow gap in this environment is a smart thing to go do. And there's going to be a lot of assets on the market. It's a very weak market and selling into that, in a significant -- and trying to raise a significant amount of money we just didn't think -- one, could you even do it? And two, is it the prudent thing to do?

But we do have some assets on the market. They're ones around the fringes of our non-core. They're typically in areas that aren't -- they're either gas or North American gas that haven't been subjected to the recent price downturn on the oil side. So you ought to still expect a little bit of disposition this year, probably less than what we had last year.

But we're still marketing our deepwater assets. We have some assets in Indonesia and in Alaska, and we're still moving those forward. But I think the point Jeff was trying to make is, if you're counting on generating multi-billion dollars of proceeds from an asset sale to bridge some cash flow gap at these lower commodity prices, we just don't think that's smart to rely on.

Evan Calio - *Morgan Stanley - Analyst*

Great. Thank you.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Evan.

Operator

Thank you. Our next question is from Neil Mehta of Goldman Sachs. Please go ahead.

Neil Mehta - *Goldman Sachs - Analyst*

Good morning, guys.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Good morning, Neil.

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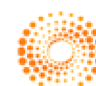

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Neil Mehta - *Goldman Sachs - Analyst*

So it looks like the reduction in capital spending, the $7.7 billion to $6.4 billion, correct me if I'm wrong, but the bulk of it looks like it's coming from the Lower 48. So I really wanted to be clear there to confirm that. And then the reduction in your production guidance, that also looks like it's therefore more likely than not coming from the Lower 48.

So I just wanted to confirm that the delta in both capex and the delta in production is primarily coming from the US. And then what does the year-over-year decline look like in your guidance for the US specifically as it relates to liquids?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Neil, you're right, the majority of the capital reduction is in the US, associated with cutting the rig count and that does result in a reduction in production in the Lower 48. We'd expect year-over-year our Lower 48 production would be about 10% lower as a result of the cuts.

Neil Mehta - *Goldman Sachs - Analyst*

And then is the -- the delta was primarily liquids, I would imagine. Because you had already assumed that there'd be a decline on the gas side.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

That's correct.

Neil Mehta - *Goldman Sachs - Analyst*

Okay. And then the follow-up, I want to explore Ryan's initial question on what's specifically changed in the oil outlook. Aside from the price on the screen, I know you have a really detailed and thoughtful economic analysis process as you think about the commodity. Was it a function of the demand? Was it a function of non-OPEC supply? Was it a function of OPEC? Was it a function of inventories? Or a combination of all those things?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

It was a bit of a combination of all those things. But we weren't anticipating a drop from $50 down to $30 like we've seen in the last seven to eight months. We would have probably expected to see inventories at this point in time starting to flatten out at least, and not continue to build, so that causes us some concern as we go into the latter half of 2016, and some concern that this might -- lower prices would extend through 2016 and the rebalancing may not occur until we get into 2017.

And then on the demand side, like everybody, we're following China and the growing markets around the world, and trying to see what the economic impact is going to be. The fourth quarter GDP in the US was quite low, largely driven by lack of investment in the oil and gas industry, driving some of that. But we have some concerns about the demand side starting to loosen a bit, as well.

Neil Mehta - *Goldman Sachs - Analyst*

All right. Thank you, Ryan.

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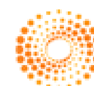

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Neil.

Operator

Thank you. Our next question is from Guy Baber of Simmons & Company. Please go ahead.

Guy Baber - *Simmons & Company International - Analyst*

Thanks for taking my question. I had a point of clarification on the decline rate that you mentioned earlier. But Matt, you had mentioned 8%, I believe. Was that for the total portfolio?

And I'm just asking because that seems high relative to the prior guidance that I thought was below 5%. So I just want to make sure that that's apples to apples and understand if there's any meaningful acceleration, and how you see the base holding up at lower spending levels.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Okay, Guy. That's an 8% base decline assuming no capital investment. No new wells to bring on any new production. So it's an unmitigated base decline, and it's consistent with what we've been saying for several years as the underlying decline in our base production. I don't think we've ever said 5%, and the range of 8% has been what we've consistently said. We haven't seen any acceleration in that.

Guy Baber - *Simmons & Company International - Analyst*

Okay, great. Thanks for clarifying that that was in the unmitigated decline. Then my second one was you all have mentioned a few times that maintaining the flexibility to respond with higher activity levels if oil prices improve.

Can you talk about how, despite cutting the rig count from 13 down to 3, you have worked or have made plans in place to really preserve that capability and those efficiencies and the ability to quickly respond to the appropriate oil price signals? And with the lowered dividend, has that price at which would you ramp up the capital allocation to the US unconventional, has that changed at all relative to the prior view?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

So we are maintaining the capacity to ramp up quickly, both in terms of preparing all the permits that we need to do that and retaining the talent that we need to do that. That's an important part of how we're managing through this downturn is retaining that capacity. In terms of the price that it would take for us to want to put rigs back to work again, it's really not a function of any specific price.

It's more a view of our price outlook as to when it would make sense. But having said that, I mean, within our Eagle Ford and Bakken portfolio, there are definitely attractive investment opportunities that have a strong rate of return at $45 a barrel or more. So although we haven't set a specific price in mind, we do have a lot of flexibility as prices recover and a lot of good places to put the capital and the talent available to make sure we're doing that wisely.

Guy Baber - *Simmons & Company International - Analyst*

Okay, great. Thanks for the color, Matt.

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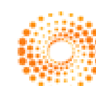

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Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Guy.

Operator

Thank you. Our next question is from Blake Fernandez of Howard Weil. Please go ahead.

Blake Fernandez - *Scotia Howard Weil Incorporated - Analyst*

Ryan, I know you've tackled the dividend pretty extensively, but my angle was a little bit different on it. I'm not surprised at the need to go ahead and cut and preserve the balance sheet. What I'm surprised about is why even maintain it at all with $45 breakeven and the current prices around $30. I'm just a little bit concerned we're not setting up for another potential cut down the road if current prices persist. Can you maybe just talk a little bit about how we should think about the ongoing evaluation of the dividend sustainability if $30 were to maintain for the next say 6 to 12 months?

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Yes, I'll jump in a little bit on that one. Part of the thought process here is that we recognize that prices could stay in the $30s for an extended period of time. And what we've done as we've set the dividend and set the capital program and looked at our balance sheet capacity is we've set things to a point where we are comfortable that we're going to have the balance sheet capacity to maintain the capital program and maintain the dividend even at prices that persist at today's level for a prolonged period of time.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

So you ask why not earlier, Blake, and we've been following this for a long time. We had a view even as much as a year ago that we would see more lower volatile prices. We've been moving the portfolio of the company into more flexibility, shorter cycle time, lower cost of supply. So it's been a view that we've been concerned about really back to the spin. But we've also seen that we didn't anticipate that it would go this low and the potential to be here for this long.

So we were surprised probably by the resiliency of the North American and the efficiencies, the economies that we've been able to drive as an industry that has kept supply going. We're surprised that OPEC has held on for as long as they have to keep their decision going. So it's been a confluence of factors. We felt like the dividend was certainly manageable at a $75 mid-cycle price. We have concerns about now how long it's going to get there, and that combined with the reduction in capacity on the balance sheet.

We still have capacity on the balance sheet. We'll use that if we need to through this lower price cycle. We just wanted to protect that and make sure we had a plan in place for a lower for longer outlook. It's prudent to plan for the downside case. We're going to do what is right for the company both in the short-, medium-, and long-term.

Blake Fernandez - *Scotia Howard Weil Incorporated - Analyst*

Got it. Okay. The next question, I want to clarify. I think you already went through the capital flexibility moving into 2017, which if I got correct was $2 billion plus $800 million on deepwater. So that pushes you toward about $3.5 billion. I'm just curious, how does that --

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Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Blake, that was $2 billion including deepwater.

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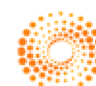

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Blake Fernandez - *Scotia Howard Weil Incorporated - Analyst*

$2 billion including deepwater. Okay, okay. Well, the question is how does that compare to slide 6 where you give a capital for flat production in the $45 world? I'm just trying to understand basically what that number is.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

So what we'd expect in a $45 world is that to maintain flat reduction over many years would take about $5.5 billion of capital. So that's what's shown on slide 6.

Blake Fernandez - *Scotia Howard Weil Incorporated - Analyst*

$5.5 billion. Got it. Okay. Thank you, Matt.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

Thanks.

Operator

Thank you. Our next question is from Paul Cheng of Barclays. Please go ahead.

Paul Cheng - *Barclays Capital - Analyst*

Hello. Good afternoon.

Before I ask my question, I just wanted to make a comment. Even though the thought may not share by many, and probably may not be totally right, but I actually wanted to compliment management and the firm making the wise choices when the market condition change, and I actually think that it will improve your long-term competitive position.

Anyway, Jeff, I think that you talk about that you still have financial flexibility, and you surely do. So to maybe eliminate a lot of concern in the marketplace, can you tell us that what is your debt capacity you can raise under a BBB rating from the current level. That's the first question.

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Paul, I don't know that we feel like we can answer that question until we get through a process with the rating agencies. Both of them have significantly reduced their price decks and talked about needing to change perhaps how they view the industry. I don't know where we're going to settle out in the credit rating bands.

The point is like I made earlier, though. We are not uncomfortable with the debt levels we have. We don't feel like it's a debt level that is going to require us to do any delevering in the future. And we do feel like we're going to have balance sheet capacity in whatever credit rating range we end up with to handle a prolonged period of lower prices like what we're seeing right now.

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Paul Cheng - *Barclays Capital - Analyst*

Jeff, do you have a minimum that what you think that you may have that capacity? We may not know for exact, but is there a minimum level you think at BBB you can raise by the debt by XYZ amount?

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

I don't know that we can really give you that kind of number currently. We do have $8 billion of liquidity. So regardless of what our rating is, we can access that capacity. I think you're asking a different question. But if you just think about how you are going to get through any near-term move, we are not in a position where we have to be concerned with our access to credit markets.

We're going to end up in this with a strong investment-grade credit rating with the balance sheet capacity to be able to continue to fund the capital program and fund the dividend we're talking about now, with a continuation of the current price environment. That's where we're -- that's the statement we are confident about making.

Paul Cheng - *Barclays Capital - Analyst*

And the second question is for Ryan. It's a little bit of the curve ball. You decided to exit the deepwater program, but with the cut in the dividend, should we be looking at that decision, whether that would improve financial and operational flexibility you should be able to maintain your deepwater program for the long haul?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

No, Paul. We made a decision and the decision to exit the deepwater was based on a look at our portfolio, a look at the cost of supply and how competitive that growth engine would be relative to what we were seeing with our unconventional portfolio and the rest of the portfolio that we have. So we think in a, regardless of what sort of mid-cycle price you return to, that we've got more opportunity existing in our captured portfolio, and that the deepwater as a growth engine won't compete against that in the portfolio.

Paul Cheng - *Barclays Capital - Analyst*

Thank you.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Paul.

Operator

Thank you. Our next question is from Roger Read of Wells Fargo. Please go ahead.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Thank you. Good morning.

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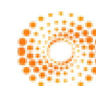

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Ryan Lance - *ConocoPhillips - Chairman and CEO*

Hi, Roger.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Just to take a look maybe at some of the incoming cash flows, thinking APLNG, the Canadian oil sands as well, as you think about current prices versus that $45, can you give us an idea of the impact of those cash flows, now to the end of this year, to maybe end of 2017?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

So at current prices, we're making capital contributions -- we expect to make capital contributions to both. At $45 a barrel, we would make capital contributions to neither. We, in fact, would be taking proceeds out of the joint ventures at those prices.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Okay. Great. Thanks.

And then as a follow-up, well it's not a cash flow, it's a net income-driven adjustment for the change in oil prices to the change in net income. Just a quick back-of-the-envelope look at it, and I'm talking about the slide here towards the end.

It looks like about a $5 difference in oil is how you cover the dividend, if I assume net income as a good proxy for cash flow. So at roughly $40, you're having to lean on the balance sheet for the dividend, and at $45 is the way we should think about the company being balanced along with that $5.5 billion capex number?

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Yes, I think we're -- we'll repeat a couple of things we said today is some calibration points for you on that. If you just look at 2016, where we said we will be balanced in terms of not needing to have additional debt, with a price that's kind of in the low $40s, but that assumes that we reduce our cash balances. That's one point.

The other point we're making that as we look longer term at the company in more of a steady state is with the changes we're making, in a $45 Brent environment, we're going to be able to have enough capital to keep flat production around the $5.5 billion that Matt referenced earlier and cover our dividend and not have any borrowings, not have any use of cash, not have any asset sales come into that. So you can just -- every dollar that the price moves above that gives us additional flexibility, as Ryan has mentioned, to either think about increasing shareholder distributions or think about increasing capital to create growth.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Okay and just the last question. Certainly you're positioning yourself for a much more, let's say, challenging market, if it hadn't been challenging enough already. Bid/ask spread on assets, you're saying is it's a bad time to be a seller. Is it at least worth now considering to be a buyer and with the dividend, let's say reduced to a more reasonable size for this oil price environment, not being really a headwind in slowing you down, and thoughts of capital allocation?

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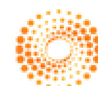

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Ryan Lance - *ConocoPhillips - Chairman and CEO*

Well, yes, that answer, Roger, really hasn't changed for the company. We watch the market. We know what we like, what we don't like, and really, the bottom line, like we've said for quite some time, is that for anything like that, it has to be competitive and substitutive in the portfolio today, and we've got a lot of low cost of supply opportunities to invest in our own portfolio that are already captured.

So we watch it. We watch it closely to make sure that there isn't anything out there that we want to slip by, but it's a pretty high competitive hurdle in the captured portfolio that we have today. So it's not been a big part, it is not a big part of our capital plans right now.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Okay, great. Thank you.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Roger.

Operator

Thank you. Our next question is from Paul Sankey of Wolfe Research. Please go ahead.

Paul Sankey - *Wolfe Research - Analyst*

Hi, everyone. Good afternoon.

You've outlined that the dividend was a differentiating factor for you, which was why we liked it so much, and it instilled a level of capital discipline. I understand that prices are now too low for that to be sustained over the long term. But I'm just wondering, why didn't you tough it out for another year?

Why didn't you just have a look for one more year? Because my concern now is that the stuff that you're talking about in debt markets, for instance, surely is going to affect many other companies much worse than you. And I'm just worried that you've kind of capitulated at the bottom if you want. Was that a consideration? Couldn't we have seen you just go one more year? Thanks.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Thank you, Paul. As I said, it was a very, very difficult decision. We looked at all those kinds of aspects. How long should we -- how long do we ride the -- when do we think the market is going to turn? And I think it's informed by a view that we had to plan for a downside case of this lower price is persistent. We're going to have a longer downturn, and that combined with reduced capacity on the balance sheet.

We had been prepared to use the balance sheet and are still prepared to use the balance sheet but we didn't think it was appropriate to take it up to the edge and destroy it, or put it in a place where we no longer had a strong balance sheet in case the worst case happened, and this was prolonged for a longer period of time. So it's informed by where we think the market is today, and the changes that we've seen with respect to the capacity we have on the balance sheet to remain investment grade.

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Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

I think I'll add to what Ryan has said. As you get to a really low price environment like what we're seeing today, I think there's a question of what your balance sheet capacity is. And there's just a question of how quickly you use up balance sheet capacity. And if you stay in the $30 price environment, I think what you are going to see across the industry is people are either going to have to be dramatically reducing their capital, or they're going to be borrowing extreme amounts of debt relative to their current debt levels. And we don't think that was an appropriate way for us to run the company.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes. Or they're going to have to sell a bunch of assets to get a bunch of money in a very down market or they're going to have to permanently destroy shareholder value and float equity.

Paul Sankey - *Wolfe Research - Analyst*

Yes, but that's my point.

These are other companies that are weaker than you. I just think that you possibly could have applied pressure, if you like, across the less strong companies if you had somewhat kept going with the policy. And I'm just trying to get my arms around the decision, and frankly, you've outlined it pretty clearly, why you've done what you've done. I just feel like it might be a bit procyclical to do it right here, right now, just before debt markets get really bad.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

I take your point, Paul.

Paul Sankey - *Wolfe Research - Analyst*

That's great.

Could you just talk a little bit about staying flat as opposed to any other volume outlook? Is that, again, people have talked a lot about this, but I'm just wondering. Is the idea now that as we go forward you are going to try to grow at a level at which you would grow the dividend, or just anything about the specific volume of being flat, what's magical about being flat? Thanks.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

I'd say, Paul, we're not trying to manage right now to a certain production level. We're trying to manage to the capital program that makes sense for the long-term value of the company, maintain our options, maintain the ability to ramp back up when it does -- and production falls out of that. Production is what production is.

I've said numerous times we're not going to drill into this headwind. Deferral makes sense. It makes economic sense. We're just trying to set an appropriate capital level to meet the commitments that we have, manage the short-, medium-, and long-term for the company, and production falls out of that.

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Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

We weren't trying to say that our expectation or aspiration is to be flat. We were just illustrating the point that at $45 a barrel, we can maintain flat production and cover the capital and the dividend. It was really to illustrate a point rather than to express an aspiration.

Paul Sankey - *Wolfe Research - Analyst*

Got it. Just finally, I've been a big fan of your analyst meetings and your disclosure. Could I just ask you, I think it's too much to ask you right here on the spot, but the slide that you have showing the breakeven of your resources obviously looks a bit scary now, because the lowest end of your band of economic resources is $45. Much of it is really set on $75. But if I could ask you to update that over the course of the next few weeks, it would be very helpful to us. Thank you.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

We'll take that on, Paul.

Operator

Thank you. Our next question is from James Sullivan of Alembic Global Advisers. Please go ahead.

James Sullivan - *Alembic Global Advisors - Analyst*

Good afternoon. Actually, picking up on that last question, I was going to look at that same pie chart myself. You had talked a couple of times and giving answers about what's going to differentiate COP going forward. You had talked about the low cost of supply and the resource base as a future differentiating factor.

Can you characterize how much of -- what the opportunity is within that resource base, whether it's PUDs or just resource for margin accretion? There were three legs of the investment case originally: moderate growth, moderate margin accretion, and the dividend, so we're not going to have growth, we're not going to have dividend. But margin accretion is possible as you replace barrels. So what's the opportunity there, especially as obviously we're seeing a cyclical decline in the cost basis here?

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

We are going through a process just now, James, of updating our cost of supply. And you're right, what we would expect to see is that the cost of supply of a lot of this resource base, all of it in fact, is going to be declining, and as a result of the deflation that we've seen across the sector. So we'll get that update sometime later in the year. We'll be ready to talk about that.

But the amount of resources available below $45 a barrel or below $60 or below $75 is growing, and as we improve our technology, and as we see deflation. So we'd expect to see that picture improve. And with a lot of diverse opportunities to deploy capital to give us both production growth and margin growth.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Yes, I would add to that, James, the basic premise when we launched as an independent company around the growth and margin and production, this reset allows us to grow off a much lower breakeven base and make decisions around that.

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The investments that we're going to make into that resource base, the basic premise that, again, that hasn't changed that resource base is still there, and it's going to represent higher margins than what the average of the total portfolio is today. So we will see margin growth, we'll see absolute growth, and, yes, we've reset the dividend a bit, but as we said all along, with a lower breakeven cost, we've got choices about how we allocate free cash flow, and we'll have free cash flow at a much lower breakeven cost.

James Sullivan - *Alembic Global Advisors - Analyst*

Okay, great. Thanks very much. We'll wait for that update.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks.

Operator

Thank you. And our last question is from Phil Gresh of JPMorgan. Please go ahead.

Phil Gresh - *JP Morgan - Analyst*

Good afternoon. Thanks for squeezing me in.

One question I have is just a clarification on the sustaining capital requirements. I think two months ago, the number was around $6.3 billion, and now it's $5.5 billion. So I was wondering what drove the reduction. And related to that, you're basically keeping production flat this year at around $6.4 billion, so I was just trying to square those two numbers.

Matt Fox - *ConocoPhillips - EVP of Exploration and Production*

What the $5.5 billion represents is essentially an adjustment of the $6 billion for the lower price environment. We said it was going to take $6 billion at $60 a barrel. When we look at our supply chain models, you can execute that same amount of scope for $5.5 billion if prices are $45 a barrel. So it's a combination of that and the efficiencies that we've seen as we've been executing our programs through 2015.

Phil Gresh - *JP Morgan - Analyst*

Got it. Okay.

And my second question is just a question around cash from operations. Deferred taxes have been a big swing factor over time, and I was just wondering, Jeff, how you would suggest we should think about that variable with the strip pricing where it is in 2016. I know there's a number of different moving pieces there and you gave us some color on the equity earnings line. But I was wondering if you could talk about deferred taxes.

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

Sure, Phil. The situation the industry, I think, is generally in right now is we don't find ourselves in cash tax-paying positions in most of the jurisdictions in which we operate. So in the past, you would have thought of deferred tax as being driven primarily between timing differences on depreciation between book and tax, but now it's really driven by the fact that when you have financial book losses, you're not able to, you don't get any cash benefit for those tax losses.

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So I would think the guidance I'd give people to think about deferred taxes is that, as you do your modeling, if you're coming to a negative number for taxes when you do your income modeling, that's going to be a negative on deferred taxes, as well because we're not going to be seeing a cash benefit from that negative tax number.

Phil Gresh - *JP Morgan - Analyst*

So is there a rough level of like $35 or $40 that you would think about generally?

Jeff Sheets - *ConocoPhillips - EVP of Finance and CFO*

No, I think it's just going to be progressive as prices improve. As you can see from when you look at results across the industry, you'll see negatives on the cash flow statement related to deferred taxes because everybody has been in these financial loss positions. As prices improve, those losses will get smaller, and deferred tax will swing around first to being less negative, then zero and then being a positive again for us in the future as prices rise. But I can't give you just exact cut-offs in prices, as far as when that will occur.

Phil Gresh - *JP Morgan - Analyst*

Okay. All right. Well, thanks a lot. I appreciate it.

Ellen DeSanctis - *ConocoPhillips - VP of IR and Communications*

Thanks, Phil. Christine, let's wrap it up here.

Operator

Okay. Thank you. And thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.

Editor

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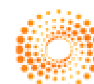

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