

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

COP - Q1 2016 ConocoPhillips Earnings Call

EVENT DATE/TIME: APRIL 28, 2016 / 4:00PM GMT

OVERVIEW:

Co. reported 1Q16 adjusted net loss of \$1.2b or \$0.95 per share.



CORPORATE PARTICIPANTS

Ellen DeSanctis *ConocoPhillips - VP, IR and Communications*

Ryan Lance *ConocoPhillips - Chairman and CEO*

Don Walleto, Jr. *ConocoPhillips - EVP, Finance, Commercial and CFO*

Al Hirshberg *ConocoPhillips - EVP, Production, Drilling and Projects*

CONFERENCE CALL PARTICIPANTS

Evan Calio *Morgan Stanley - Analyst*

Doug Leggate *BofA Merrill Lynch - Analyst*

Neil Mehta *Goldman Sachs - Analyst*

Phil Gresh *JPMorgan - Analyst*

Blake Fernandez *Scotia Howard Weil - Analyst*

Roger Read *Wells Fargo Securities - Analyst*

Doug Terreson *Evercore ISI - Analyst*

Guy Baber *Piper Jaffray - Analyst*

Paul Cheng *Barclays Capital - Analyst*

Edward Westlake *Credit Suisse - Analyst*

Paul Sankey *Wolfe Research - Analyst*

Scott Hanold *RBC Capital Markets - Analyst*

James Sullivan *Alembic Global Advisors - Analyst*

Pavel Molchanov *Raymond James & Associates - Analyst*

Asit Sen *CLSA - Analyst*

PRESENTATION

Operator

Welcome to the first-quarter 2016 ConocoPhillips earnings conference call. My name is Christine and I will be your operator for today's call. At this time all participants are in a listen-only mode. Later we will conduct a question-and-answer session. Please note that this conference is being recorded.

I will now turn the call over to Ellen DeSanctis, VP, Investor Relations and Communications. You may begin.

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

Thanks, Christine, and good morning to everybody. Again, thank you for joining our first-quarter earnings call. Our speakers for today will be Ryan Lance, our Chairman and CEO; Don Walleto, our Executive Vice President of Finance and Commercial and our Chief Financial Officer; and Al Hirshberg, our Executive Vice President of Production, Drilling and Projects. Ryan will cover the company level comments, Don will then review the quarterly financials and Al will review the operational highlights for the quarter and our outlook for the rest of the year.



Before we start I wanted to let all of you know that we have set a date of November 10, 2016, for our analyst and investor meeting, this year's analyst and investor meeting. The event will be held in New York and we will provide some additional details soon. We just wanted to make sure that you got that on your calendars.

Finally, we will make some forward-looking statements this morning. The risks and uncertainties in our future performance have been described on page two of today's presentation as well as in our periodic filings with the SEC. And of course that information, in addition to some supplemental data for today's earnings, can be found on our website.

Now it is my pleasure to turn the call over to Ryan.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Thank you, Ellen, and thanks to all for joining the call today.

Before I jump into the quarterly results, I want to make some general comments about the company and the environment that we find ourselves in today. On the next couple of slides, I will address how ConocoPhillips is positioning to create value as an independent E&P company. I will describe our value proposition and how we will compete in a world of lower mid-cycle and more volatile prices. I will also describe how we are prioritizing our business activities in the short term, the medium term and the long term.

I think it is important for investors to know how we are thinking about the current environment, but also how we have positioned the company for strong performance when prices recover. So if you please turn to slide 4, we will get started.

We believe that our value proposition lies in the combination of our unique portfolio attributes and our capital allocation principles. Let me start with the left side of this slide. Underlying our value proposition is a portfolio that we think is quite unique among E&Ps. We have listed several attributes that distinguish our asset base.

We have a diverse, relatively low-decline base of production. We expect our decline rate to moderate somewhat over the next few years as we bring on additional tranches of low to no decline oil sands and LNG projects. Growth will come from investments in our large low cost of supply resource base. We continue to analyze and calibrate this resource base as we believe it holds profitable investment inventory to keep production or grow modestly, keep flat production or grow modestly for well over a decade.

Within this captured resource base, we have a mix of flexible, short-cycle projects and lower risk, medium-cycle investment projects. We see a role for both of these types of assets in our portfolio. And finally, the key to being successful in a cyclical business is to have a sustained low-cost structure.

On the right side of this slide are the capital allocation principles that describe our value proposition. Conceptually, the principles are similar to the ones we had at the time of the spin, namely, give cash back to shareholders, maintain a strong investment grade balance sheet and exercise disciplined growth. Obviously these elements have been reset, but this is still how we expect to deliver returns to the shareholders.

Now let me go through these principles. We reset the dividend, but we still intend to return a meaningful portion of our cash back to our shareholders through a cash dividend. In February, we set the dividend at a level that we believe can be sustained through the price cycles but that also results in a competitive yield compared to the broad market as well as to the E&Ps. The dividend will remain a core part of our offering and we are targeting annual real growth in that dividend going forward.

We remain committed to have a strong investment-grade balance sheet. The recent downturn has emphasized the importance of a strong balance sheet. We have set a target to get our debt to less than \$25 billion. The pace of that debt reduction will depend on prices and asset sales progress, but de-levering is a top priority as we come out of the downturn.



We have positioned the company to compete on financial returns. So despite having a large, low cost of supply portfolio, we won't grow for growth's sake. We will continue to be very disciplined about how we allocate our growth capital. We are in a strong position to do that as we come to the end of a significant major project investment phase. You will notice that we are stating that our growth could be on an absolute or per-share basis.

Again, the financial returns are at the core of our value proposition. If we get the returns right, the rest will follow. We are committed to getting the returns right.

So the way we think about creating value through the cycles is to have clear principles that align with a competitive portfolio to generate strong returns for the shareholders. One without the other is not sufficient and we believe we have both. We believe we have a sound value proposition, but what also matters is how we are executing our value proposition for the short, medium and long term. It is important to be disciplined across all three time horizons especially coming out of this price downturn. I will cover this on the next slide.

First, the short term. For us, it is all about defending against low prices in 2016 and 2017. In the first quarter, we raised \$4.6 billion of low-cost debt. We announced this morning that we are further cutting 2016 capital from \$6.4 billion to \$5.7 billion. We reset the dividend for the lower end of the price cycle, we have strong liquidity, including about \$5 billion of cash on hand at the end of the first quarter.

We think we took the right short-term steps to protect against an extended period of weak prices. At the same time, we are staying disciplined and continuing to safely execute our operating plan and AI will provide more details about that in a moment, but we are running well and our key projects are on track.

Finally, we are focused on lowering the breakeven cost of the business. Now for perspective, if we were in a steady-state world of sustained \$45 per barrel oil prices, we believe we could cover the capital required to maintain flat production and pay our dividend with cash from operations. Now this steady state for us comes after completion of our major projects and a reallocation of capital to our low cost of supply conventional and unconventional portfolio.

This positions us to accelerate performance as prices improve in the medium-term. Debt reduction will be a priority and we will target growing the dividend on a real annual basis.

We remain focused on safely executing the business. We will complete several major projects in the medium-term that will ramp up production from those projects. Finally, when prices start to recover, it will be important to stay diligent on our cost efforts.

Our long-term goal is to execute predictable performance in a world of lower, more volatile prices. We can do this by achieving our target debt level and striving to maintain cash flow neutrality.

Now we defined cash flow neutrality as capex for flat production plus our dividend equals cash from operations. As we generate cash in excess of cash flow neutrality, we have choices about how to allocate those funds. We can return cash to shareholders through share repurchases or we can fund more investments in our low cost of supply resource base. Growth capex will compete with distributions to shareholders. That means we are not setting a target for absolute growth because we are willing to grow on a per-share basis if that makes more sense.

We will continue to high grade the portfolio and those proceeds will be allocated to debt reduction, distributions and capex. We can also choose to keep additional cash on hand, especially if we thought another low-price cycle was approaching. The decisions on how we allocate the cash flows will be based on staying disciplined, achieving the best returns and maximizing value for shareholders. Certainly the last 18 months have really brought home some fundamentals for how to thrive in a cyclical business.

We believe it is essential to have a high degree of capital flexibility, a low cost of supply portfolio, best-in-class cost structure and a strong balance sheet. Most of all you have to be disciplined. The way to win in a cyclical business is to have a low cost of supply portfolio and to be the most resilient when prices are low and the most disciplined when prices are high.

Now I hope these short comments were helpful. But on slide 6, I will summarize the results for the quarter.



The left column recaps the strategic actions that I have just described. The middle column captures our operational highlights and Al will discuss those in a bit more detail. We met our goals and our important capital programs are progressing well. The right column summarizes the financial results for the quarter. There is no getting around it, it was a very weak quarter financially. Underlying performance on the things we can control, like operating costs, were strong, but the bottom line was a large adjusted net loss that clearly reflected the weak commodity price environment.

So now let me turn the call over to Don for a few comments on our financial results.

Don Wallette, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

Thanks, Ryan. I will start with our first-quarter adjusted earnings on slide 8. As Ryan mentioned, we had a strong quarter operationally, but low commodity prices continued to dominate the quarter's financial results. We reported an adjusted net loss of \$1.2 billion, or \$0.95 per share, with realized prices down 20% sequentially and 38% year-over-year.

First-quarter adjusted earnings by segment are shown in the lower right side of the slide.

Our segment adjusted earnings are roughly in line with expectations. The supplemental data on our website provides additional financial detail. The only notable item to call out this quarter is in the Lower 48 where earnings were negatively impacted by approximately \$70 million as a result of a dry hole at the Melmar prospect in the Gulf of Mexico.

A couple of other items of note. While we have lowered capital guidance, we are not changing any other guidance items at this time. This includes operating expense, which ran light to expectations this quarter. We expect to give you an update at midyear.

Also, we have updated our sensitivities in the appendix of this deck. We changed Henry Hub to reflect the impact of last year's asset sales, and WTI to reflect production decline in the Lower 48 due to reduced drilling activity.

Turning to slide 9, I will cover production. First-quarter production averaged 1.578 million BOE per day, which was the upper end of guidance reflecting increased ramp at APLNG and better performance across the portfolio. Last year's first-quarter volumes were 1.61 million BOE per day, but after adjusting for dispositions first-quarter 2015 volumes would be 1.54 million BOE per day. As a reminder, the majority of those dispositions were natural gas properties so as a result, North American gas represents only 19% of our overall production this quarter compared to 24% in the year-ago period.

Continuing through the waterfall and netting out the differences in downtime, we saw an underlying increase of 34 thousand BOE per day, or 2%. That increase came primarily from APLNG gas and Canadian bitumen, partly offset by a decline in North American gas. This gets you to 1.578 million BOE per day production for the quarter. So underlying performance is strong.

If you turn to slide 10, I will cover the cash flows during the quarter. We started the year with \$2.4 billion in cash and generated \$700 million from operating activities, excluding working capital. Working capital was an offset of about \$400 million in the first quarter, but we expect it to be a wash for the full year.

During the quarter, we received about \$100 million of net proceeds from dispositions. Net debt increased by \$4.5 billion and capital spending for the quarter was \$1.8 billion, which we expect to be the high watermark for the year.

After dividend payments of \$300 million, we ended the quarter with \$5.2 billion in cash and short-term investments. It was a tough quarter financially, but we ended the quarter with a significant amount of cash on hand and strong liquidity to manage through the price environment. We can't do much about prices but the key is to continue executing the business well and we are doing that as you will now hear from Al.



Al Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

Thanks, Don. I will provide a brief update on each of our operating segments and then we can move on to your questions. I will start with the Lower 48 and Canada segments on slide 12.

In the Lower 48, our production in the first quarter was 491 thousand barrels of oil equivalent per day. That is down 15 thousand barrels per day, or 3%, compared to our first-quarter production last year once you adjust for asset sales. The reduction is primarily due to our reduced rig count last year, which is impacting our production this year. We further exercised our capital flexibility in the Lower 48 and dropped down to three operated rigs in April and we plan to stay at that level through 2016.

Now that said even with the lower rig count, we are continuing to realize strong efficiencies in the Eagle Ford and Bakken and we will keep leveraging technology and working with our vendors to improve performance and capture deflation where possible.

In exploration, the non-operated Gibson well is currently drilling. However, that is the last exploration well that we plan to drill in the deepwater Gulf of Mexico. In this price environment, we don't feel it is prudent to continue allocating capital to new deepwater prospects, so we no longer plan to drill Horus or Socorro, which we had planned to drill with the Maersk Valiant drillship.

By the way, these changes account for about half of our 2016 capital reduction from \$6.4 billion to \$5.7 billion that Ryan referred to earlier.

Looking at Canada, our production was 293 thousand barrels per day. That is an increase of 2% compared to the first-quarter 2015 production of 288 thousand after adjusting for dispositions. The increase is driven mostly by improved well performance in western Canada and ramp up at Surmont 2. In the past year we have increased our bitumen production by 6 percent and reduced underlying gas production by 3 percent. But when you include asset sales though, gas is down 23 percent, so we have significantly changed our production mix in Canada.

So moving over to slide 13, I will cover the Alaska and Europe and North Africa segments. These regions have many of our legacy assets that still compete for capital. As you can see, the low cost of supply projects we brought on line over the last couple of years are beginning to offset natural declines. In Alaska, we are seeing favorable results from our CD5 and Drill Site 2S projects, which both started up in the fourth quarter of last year and are contributing to a 3 percent production increase over the first quarter of 2015.

We also just approved an additional phase at CD5, which will bring more wells online in late 2017. We are starting activity at GMT1, which was sanctioned at the end of 2015 and is expected to come online in late 2018.

In Europe, production is also up 3 percent versus the first quarter of 2015 and we have several more projects underway, which are expected to start up over the next couple of years. In late 2015, we successfully took over operatorship at Britannia, which was previously operated by a joint venture. We are seeing cost savings from this action and it is a good example of efficiency improvements that we have been able to implement.

Slide 14 covers our last two segments, Asia Pacific and Middle East and Other International. In APME, production is up 36,000 barrels oil equivalent per day, or 10 percent, year-over-year primarily as a result of the ramp up at APLNG. Train 1 is running well and ramped up more quickly than anticipated with 11 cargoes loaded in the first quarter. And as of earlier this week, we have actually now loaded 15 cargoes at APLNG.

In Malaysia, we are ramping up at Gumusut after starting up the gas and water injection and we are continuing to progress the Malikai project which should start producing next year.

As the Other International segment is exploration focused, the main news for the quarter is from Senegal where we completed several successful appraisal wells and drill stem tests to further evaluate this new play opening discovery.

So Ryan started the call with details of our value proposition and strategy and then Don covered the financial results. If you will turn to slide 15, I will wrap up with our operational outlook for the year.

While we continue to focus on lowering capital and reducing costs, we are committed to safely delivering on our operational commitments. As we previously guided, we expect our 2016 production to be essentially flat to 2015 when you exclude the full-year effects of asset sales. This result is driven by some decline in the Lower 48 unconventional as we continue to exercise our capital flexibility there, offset by growth in the other segments.

In the second quarter, production is expected to be between 1.5 million and 1.54 million barrels per day. The reduction from first quarter is the result of major turnaround in activity we have planned, primarily in Europe. Turnaround activity will continue into the third quarter, mostly in Europe and Alaska. By the fourth quarter, we expect production to increase as our major turnarounds are completed.

We are continuing to ramp up at Surmont 2 in Canada and have ongoing project developments in Alaska, Europe and Asia Pacific that will also add to production.

Finally, in Australia, we expect to deliver the first cargo from APLNG Train 2 in the fourth quarter of this year.

So the price environment continues to be challenging but as always, we will continue to focus on the things we can control: delivering best-in-class safety performance, bringing our projects online on time and on budget, and meeting or exceeding our operating targets.

So now I will turn the call over for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Evan Calio, Morgan Stanley.

Evan Calio - Morgan Stanley - Analyst

Good afternoon, guys. Let me start off with a macro question. On the last call you talked about potentially adding rigs into 2017 in the Lower 48. I know it is a complicated formula but is there a threshold commodity price that you need to see to add in 2017 given spending and de-leveraging objectives? How do you think about that?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Evan, this is Al, I will take that one. I guess first, I should say that as I said earlier, we don't have any plans to add any rigs beyond the three that we are running in the Lower 48 in 2016. And of course we haven't set our 2017 budget yet so we haven't determined how many we would run there. But overall I would say that there is no set spot price that we are trying to watch as a trigger to start adding back activity. We will be looking at the entire macro environment, looking at supply and demand fundamentals and whether we think that any price action that we get is actually sustainable or not.

And then as prices do come back, our first priority is going to be to strengthen the balance sheet, reduce our debt. And then even after that, we recognize that adding capital for organic growth is going to have to compete with other things on our list like, for example, per-share growth. So we are not in a hurry to say there is some price trigger where we are going to add back capital.

Evan Calio - Morgan Stanley - Analyst

So I think as a follow-up, I think in 3Q you mentioned you need 16 rigs to hold unconventional production flat and now you are at three. What is your implied unconventional decline or Lower 48 decline in your guidance?



Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

If you look at the overall decline say full-year 2016 to full-year 2015, we expect it to come in around 10% with the rigs that we are running, with the three rigs.

Evan Calio - Morgan Stanley - Analyst

Great, I will leave it there. Thanks, guys.

Operator

Doug Leggate, Bank of America.

Doug Leggate - BofA Merrill Lynch - Analyst

Thank you. Good morning, everyone. I have to say I love the per-share focus, Ryan. A couple of questions if I may around that.

First of all, on the debt metrics, do you have some kind of measure you are using whether it be net debt to capital or EBITDA coverage or something like that that you are aiming to get to? Because I think Jeff said in the last call that you were happy around \$25 billion. Obviously it is a little higher than that now so is there some framework you can give us as to where you want the balance sheet to get to before you perhaps embark upon buybacks?

Ryan Lance - ConocoPhillips - Chairman and CEO

Don has got some comments there, Doug. If you could?

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

Yes, Doug. We are trying to send a very clear message that we don't want to be carrying balance sheet debt of nearly \$30 billion and so this is the reason why we have set a very clear, specific goal to bring that down to below \$25 billion. We think for a company our size and diversity we are comfortable with the coverage provided across a range of mid-cycle prices with that level of debt.

Doug Leggate - BofA Merrill Lynch - Analyst

Okay, so there is no specific metric like an EBITDA multiple or something like that that you are targeting?

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

No, we are targeting going down to a specific debt level and that sort of has an implied debt to cash flow type multiple depending on what sort of mid-cycle price you want to look at.

Doug Leggate - BofA Merrill Lynch - Analyst

Okay, great. Thank you. My followup is, I think, Ryan, there are still -- or maybe Don, there is still probably some confusion around what your sensitivity looks like to the commodity. I mean in your appendix of your slide deck you are sticking with earnings sensitivities, but I wonder if you I could ask you to walk us through what happens at the cash flow level assuming there is some kind of recovery in the commodity at some point?

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

Yes, sure, Doug. I think obviously at these products prices that we are at now, we are not in a tax paying position, so the sensitivities as you would have applied them a few years ago to try to convert from net income to cash flow no longer apply. So the simplest guidance that I can give you is just take those net income sensitivities and gross them up for the tax impact. So if you divide by 0.6 then that will make a conversion. As long as we are not in a taxpaying position.

Doug Leggate - BofA Merrill Lynch - Analyst

Up to what level? Is that like up to a \$60 level or can you frame that for us?

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

This is a very complex question because we are operating in so many different tax jurisdictions and it depends a lot on the price path that you take to get to that number. It is going to be different all across the company. But I think in general terms, \$60 is probably a pretty good guess overall for the corporation.

Doug Leggate - BofA Merrill Lynch - Analyst

Great. I will leave it there. Thank you.

Operator

Neil Mehta, Goldman Sachs.

Neil Mehta - Goldman Sachs - Analyst

So on the reduction in capital spending, I think you called out a couple of items in the quarter but just wanted to make sure I got all of it. So the drivers that got you down to \$5.7 billion from the \$6.4 billion, if you could just help us -- walk through that. And then does that impact the way you think about the \$6 billion you need to keep production flat in a \$60 world?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

The \$0.7 billion of reduction just about half of that as I mentioned earlier comes from the reduction that we are taking earlier on the deepwater Gulf of Mexico by not drilling Horus and Socorro. The next biggest item after that actually is additional deflation beyond what we had already assumed in our numbers and then beyond that, it is all smaller things around the world in different places, APLNG, China, Indonesia with some small reductions. APLNG is a joint venture because we've got some extra cargoes over what we had anticipated because the plant is running so well. That extra revenue has us putting a little less cash in there.

So it is things, smaller things like that that add up to the rest of that to get us to that \$5.7 billion. So none of those things are going to have any impact on 2016 production, only a very tiny impact on 2017 production, some of those small deferrals.

As far as the way you think about how much capex it takes to stay flat, the only thing on that list that might impact that a bit is just the deflation. We are still in that \$5 billion to \$6 billion range of what it is going to take to stay flat over a long period of time. Ryan talked about 10+ years in our resource base in a \$5 billion to \$6 billion real kind of capital per year that we can hold production flat.

Ryan Lance - ConocoPhillips - Chairman and CEO

Yes, at the kind of prices that you quoted, Neil.

Neil Mehta - Goldman Sachs - Analyst

That is great. I know as part of the work that you are doing into the analyst day you are doing an economic analysis to figure out the cost of supply and the returns of different parts of your portfolio. Can you just talk a little bit about how shale competes relative to some of the other non-OPEC projects outside of the US as you think about where it is best to deploy capital both on the cost of supply but then also on a cycle-time basis?

Ryan Lance - ConocoPhillips - Chairman and CEO

Yes, I think we referred to that a bit in my opening comments. We really have been working pretty hard to position the portfolio over the last couple of years into shorter cycle-time investments. And when we look at the cost of supply across our portfolio, the things that we think compete really well against any investments globally around the world are some of our conventional legacy investments around China, Alaska, Norway, UK, Malaysia. And then our unconventional investments, which I think was more of the point of your question around the Eagle Ford and the Bakken, while they could have a gross wide range of cost of supply, if you are in the best rocks like we are and in the positions that we are, those costs of supply are very competitive with anything that we have got or any non-OPEC kind of investments that you refer to around the world today.

So we will talk a bit more about that in the analyst meeting that Ellen referred to coming up to show you. Even within our portfolio, there is a range of cost of supply around each asset. But we are getting to a place where we understand that very well so we can make sure that we are very disciplined in terms of how we allocate the capital to the highest returning, lowest cost to supply assets in the portfolio.

Neil Mehta - Goldman Sachs - Analyst

That is great, Ryan. Thank you.

Operator

Phil Gresh, JPMorgan.

Phil Gresh - JPMorgan - Analyst

Good afternoon. First question was I think a follow up to Evan's question where you were talking about reinvestment. And I think in the last call you talked about a roughly \$2 billion of roll off spend from 2016 to 2017 that could be used to reinvest and potentially keep production flat. But you also mentioned now that you are not in a hurry to add rigs in unconventional. So I'm just trying to square those two items and how we should be thinking about that flexible capital. I assume that flexible capital also slips down a little because you pulled some of that forward with the deepwater decision this quarter.



Al Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

Phil, that is exactly right. The \$2 billion is what we were talking about before. And with the step down, that number is now about \$1.5 billion/ \$1.6 billion. It is in that range of roll off from 2016 to 2017. So that is still there. You can roughly think of that about \$1 billion of it is from APLNG and FCCL and about \$0.5 billion from the deepwater.

But then there are some offsets in our base plan. We have some of these mid-cycle size projects that we have executing that are going to be bringing us volumes over the next few years that are in a phase in their life where their capital is actually going to be increasing 2016 to 2017. And that is close to \$1 billion. So that is things like Bohai Phase 3 in China, Clair Ridge, GMT1 1H News, Aasta Hansteen, some of those kind of mid-size projects are going to use some of that.

That still leaves on the order of \$0.5 billion of additional flexibility that we will have, but at the end of the day we still expect that between \$5 billion and \$6 billion is what it would take to hold production flat over the coming years.

Phil Gresh - *JPMorgan - Analyst*

Okay, got it. My follow up is with respect to the balance sheet piece that you were talking about, \$25 billion target I assume over time. You also have a fair amount of cash on the balance sheet so I was just trying to understand minimum cash requirements and roughly how quickly in a strip case you feel like you could get to that \$25 billion target or do you have a goal around that?

Don Walleette, Jr. - *ConocoPhillips - EVP, Finance, Commercial and CFO*

This is a medium-term priority that we see occurring over time as prices recover. We do have a good cash balance. We are looking at using some of our cash balances to reduce our debt balances and you may see some of that activity as early as the current quarter. Then come October of this year, we've got a maturity of about \$1.25 billion and so that will provide another opportunity. But that is something that we will look at later in the year and that will depend quite a bit on our financial position at the time, how much leverage we are comfortable carrying and probably most importantly our outlook on product prices over the short term, over the next year or so.

Phil Gresh - *JPMorgan - Analyst*

Okay, makes sense. Thanks.

Operator

Blake Fernandez, Scotia Howard Weil.

Blake Fernandez - *Scotia Howard Weil - Analyst*

Good morning. I have two questions. I guess both really on shareholder returns. The first one I guess getting back down to that targeted debt level. Once we do get to free cash flow neutrality and then really in excess cash flow, is it fair to think that the primary target will be reducing debt over and above shareholder returns vis-a-vis dividend increases and/or buybacks?

And then I guess a second question I will just go ahead and ask them both. Are there any specific metrics you are going to be evaluating on buybacks versus reinvesting into the business? I guess I'm trying to get a sense is this going to be more of a ratable type of program or more opportunistic depending on where the equity price sits at the time?



Ryan Lance - ConocoPhillips - Chairman and CEO

I'll take the first one, when you look at what we set as priorities, we've got clearly in the medium-term we need to get the balance sheet repaired and back down to the target levels that Don described. But at the same time, we think we are going to target annual real increases to the dividend at the same time. To put that in perspective, a 3%, 4%, 5% dividend increase is less than \$60 million. So I think we are going -- that will be important to us to demonstrate that as well as we are going forward.

So we will be targeting some of those annual returns to the shareholders through the dividend channel and also reducing the debt as we come out of an area where we are generating free cash or we have reached that point of cash flow neutrality that you referred to.

Now as we get that free cash and we think about it, what we have said is we are just going to be just really judicious about allocating the capital, making sure that per-share growth competes with organic growth that we have in the portfolio. I think we will probably be a bit less ratable, we will try to be a bit more opportunistic around that.

Blake Fernandez - Scotia Howard Weil - Analyst

Great. Thank you, Ryan.

Operator

Roger Read, Wells Fargo.

Roger Read - Wells Fargo Securities - Analyst

Thanks, good morning here in Houston still anyway. Quick question for you on the opex side obviously ahead of pace Q1 not changing target for the full year and kind of coming with some of the questions asked earlier about oil prices recovery, you start maybe spending more on capex, reducing debt. What is your outlook for the opex side? Is this a sustainable level or is there an inflation that's got to come back or some deferrals that are likely to hit in 2017 or 2018 that won't occur in 2016?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Roger, I will take that one. First, to just remind us where we have been. Go back to just one year ago in April of 15 at our analyst day we were talking about being at \$9.7 billion of opex in 2014 and we set a \$1 billion reduction target and we beat that in 2015 by coming down 1.7, down to 8. And then we have taken another \$1 billion out in our target for 2016 and as you correctly point out if you look at the first quarter number and multiply it by four, you get a number that is less than \$6.5 billion. So we were on a really good pace in the first quarter.

Our operating and our technical teams and our supply chain folks have really been successful at driving out costs. The focus in all that work as you were kind of hinting at has been on sustainability, finding sustainable reduction, structural reductions while also capturing as much of the cyclical as we can even though we know we will have to give some of that back at the end of the day.

So frankly I do expect to beat \$7 billion this year, but we have got these turnaround season coming, there is also the Horus and Socorro decision, that rig was going to be on capex and we will have about an incremental \$100 million of opex as we have a stacked rig there.

And so our organization is going to continue working. We've got a lot of work going on to continue working on opex and I expect that we will beat that number but really at midyear I think we will be ready to update where we are going to land.



Roger Read - Wells Fargo Securities - Analyst

Okay, thanks. And then my other question - asset sales, obviously not much in Q1. Everybody knows about the giant backlog out there, but any progress at all you can hit towards -- for this year?

Ryan Lance - ConocoPhillips - Chairman and CEO

Yes, I will take it, Roger. I think we said throughout the year is we ought to be able to divest \$1 billion to \$2 billion. We will probably be on the lower end of that. I think what we showed in the first quarter was \$100 million, and I think we are pretty close to doubling that as we look forward kind of over the next quarter in terms of things we've got in the process to close. But it will probably be the lower end of that.

We've pulled some assets off the market where we are not getting what we think is fair value for it, but there are a few more assets that we still have on the market that we are hopeful around.

So I think we will be at more than what we showed certainly in the first quarter, but we may not hit that full \$1 billion mark that we were trying to hit at the beginning of the year. The market has just softened quite a lot, as you describe.

Roger Read - Wells Fargo Securities - Analyst

Great, thank you.

Operator

Doug Terreson, Evercore ISI.

Doug Terreson - Evercore ISI - Analyst

I was off for a few minutes, and so if you've covered my question, just let me know. First, I think Ryan and Al made pretty clear that there is going to be a shift and emphasis away from growth and towards returns on capital with distributions to shareholders important too, although that has always been the case for you guys.

So my question is whether the company plans to use specific metrics such as capital expenditures per unit of shareholder distribution, or some other metric that you deem important, to manage to the objectives over the next couple of years just to ensure that the capital management plan is kept in the boundaries.

Or put another way, the question is really how in practice will you execute this plan and keep us abreast of the progress? So how are you thinking about that?

Ryan Lance - ConocoPhillips - Chairman and CEO

Yes, Doug, I guess probably not a real precise formula in how you go through that. A lot depends on how fast and the slope of the recovery as we go forward, how quickly we can get the balance sheet down to the target levels that we are talking about. But I think what we tried to describe to people is we, as the price does turn and we get above a breakeven price, we start generating that free cash flow.

What we have said is we think we ought to be investing in short- and medium-cycle projects. We ought to be real returns back to -- annually real returns back to the shareholder through the dividend channel, and then just paying pretty close attention to where the stock is trading in the

marketplace, how we think -- is it an undervalued stock so we can look at the returns that we might get on a per-share basis, and compare that to the cost of supply and the opportunity to invest in the organic side of the portfolio.

We've got a pretty deep inventory of things to choose from. We know we've got a range of cost of supply sitting in that portfolio as well. But we probably won't have an exact formula, we won't make a declaration about how we are doing it, but we will certainly report how we are doing that quarterly to you.

Doug Terreson - *Evercore ISI - Analyst*

Okay, I think a better balance would be welcomed by the market for everybody. So I think that is good news. Also, Ryan, in Canada, I wanted to get your insight into the opportunities you see from a solvent technology that has begun to become available. Meaning is this something that you guys are optimistic about for your portfolio? Are you employing it already? What do think the opportunity is there for the company?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

Well I think it is part of our effort to get cost of supply in the oil sands down to something that is competitive in the portfolio. AI might have more detail on that, more current detail anyways. But in any case, I would plan to provide a lot more detail about that in November, but I will let AI jump in as well.

AI Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

I think you've probably seen some things out there in the industry being talked about around that technology, Doug. We are excited about it also. We call our version of it e-SAGD. And we have run a few pilots going back quite a few years to try to optimize the way we use that technology and it definitely works. It is a methodology to lower your steam oil ratio and also to thereby reduce your greenhouse gas emissions per barrel of production and so it has got a lot of attractiveness to it.

One of the key variables is just the solvent recovery and how much of that solvent do you get back versus having to put more into the ground. That is some of where we have had our focus, but I think we will probably have an opportunity to address where we see that headed, that technology along with some others, at our analyst day in November.

Doug Terreson - *Evercore ISI - Analyst*

Okay, great, AI. Thanks a lot.

Operator

Guy Baber, Piper Jaffray.

Guy Baber - *Piper Jaffray - Analyst*

Thank you guys very much for taking my question. AI, you highlighted the declines for the US unconventional volumes. With another quarter under your belt now running at three rigs, your latest view on deflation capture and efficiencies. Do you have an updated view as to the level of capital or the amount of rigs you would need to redeploy into the US to reverse that decline and to begin to grow that production?



Along those lines with the activity reductions that have taken place for you, the headcount that we have lost more broadly across the service sector, can you just discuss for us the lead times that may be developing for you to begin to pivot from reducing rigs back to increasing activity levels? And how do you think about preserving that flexibility to ramp up over time?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

I should have written all those questions down. I will try to catch them all. First, on supply chain, let me just mention our overall progress there. We talked at our analyst day a year ago about trying to get \$1 billion of -- that is both capex and opex -- of supply chain savings and we did achieve just a little over that in 2015 of deflation savings, capex and opex, from our supply chain. And then we set a target for ourselves for this year to get another \$1 billion and so far we are on track with that.

If you look at actually captured deflation savings in 2016 for us in the first quarter, it was \$300 million, that is capex and opex. So we are on track there and in fact are starting to think about our window of opportunity for locking in some of these prices for longer periods of time going forward as we think about what our cost structure is going to look like as things start to come back.

In terms of the rigs that we need -- let me just talk about say the rigs that we need to hold flat. So we are down to three rigs in the Lower 48 right now. We would need to get back up to 12 to 13 rigs somewhere in that range in order to just get back to holding our production flat and a number higher than that to start growing our production again.

We have retained the capability amongst our staff to be able to do that and so from our internal standpoint, we can do it relatively quickly if that is what we chose to do. From an external standpoint obviously, there has been a lot of loss of both hardware capability and people capability amongst our contracting community. And so I think the first leg of returning some rigs back to work is going to be something that can be done in a fairly short amount of time but similar to us where we go from three to 12 or 13 to hold flat, to go to that even bigger number to grow, with the whole industry is trying to do that at once, I don't think that capacity is going to be there. And so it will have to be built up over time and I can see that being north of a year, one to two year kind of timeframe to really build that kind of capacity back.

In other words, I don't think US unconventional production can go back up as fast as it came down or is coming down still.

Guy Baber - Piper Jaffray - Analyst

(multiple speakers) Thanks for those comments, Al. And then my second question, even though the first one I guess had multiple parts -- is the view now that longer cycle time greenfield projects are no longer necessary for Conoco to hold the production flattish longer-term through the cycle at that \$5 billion to \$6 billion of capex?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Yes, that is exactly right. That is one of the conclusions that we have reached is that as we look into that deep set of resource-base, low cost of supply, we are going to show you more about this in November just how much that cost supply has come down. It is dramatically lower than the cost of supply numbers that we showed you last April. And so it gives us that deep bench of anywhere from shorter cycle to medium cycle sort of sized projects that allows us as we look out well over a decade to hold production flat at this \$5 billion to \$6 billion kind of range without needing any megaprojects or long cycle projects to do that.

Operator

Paul Cheng, Barclays.



Paul Cheng - *Barclays Capital - Analyst*

I think I have two questions. The first one is probably for Don and Ryan. In terms of your medium-term target for the debt reduction, \$25 billion, I am just curious given the industry it seems like every time when we have a major downturn the industry caught by surprise. At \$25 billion, certainly at a reasonable oil price environment, you are more than comfortable to handle it but given that our ability to predict the turn of the cycle are close to zero or at least that is the track record. So should we target the debt reduction to be significantly more than that? And in the sense that you position yourself, yet indeed, we got caught by surprise and have a major downturn not only you won't be getting into any financial distress but you also could take the opportunity be a buyer and not a seller.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

I think we are going to be looking at all those items so when we say less than \$25 billion, that is exactly some of the thoughts that are on our mind is how do you prepare for the next down cycle because that we think we need to set up the company to be successful in a lower mid-cycle price with more volatility. The added comment to the balance sheet piece is certainly we will be watching that and trying to decide but we are setting ourselves up with a lot of capital flexibility in these shorter cycle time projects.

So it is not just there is going to be other ways to manage the cash and at the end of the day once we hit free cash flow we've got a lot of choices about how to allocate that free cash flow, some of which may be keeping cash on the balance sheet and preparing. So it is about net debt, it is not just the balance sheet debt is there but yes, we are going to be trying to factor that all in in conjunction with both our short- and longer-term outlook on commodity prices.

Paul Cheng - *Barclays Capital - Analyst*

Second one, real quick in the past you provide what is the Eagle Ford and Bakken production. Just want to see whether you would be able to provide that for the first quarter and also the split between oil and gas in those production?

Al Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

I guess the first quarter production at Eagle Ford was 168 thousand oil equivalent barrels per day. I don't know if you have the split?

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

Paul, I can come back to you on that.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

I'm not sure we have the split at our fingertip, Paul.

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

I don't have it at my fingers but I can come back to you on that, Paul.

Paul Cheng - *Barclays Capital - Analyst*

Okay, thank you.



Operator

Edward Westlake, Credit Suisse.

Edward Westlake - Credit Suisse - Analyst

Yes, good morning. I guess we will be dealing with this maintenance capex question again. I mean I can see how you have spent a lot of money on these long life projects which tend to have higher upfront capex. I can see how shale could be more efficient. I can see how things like Bohai and Aasta Hansteen and some of the conventional projects would be lower and I'm looking forward to the analyst day.

But the question I have is around how much deflation or inflation have you included in the projection as you go out over time, because obviously the market is starting to think oil is going back up. At some point that may mean costs go up. So maybe just a current comment on deflation in those types of assets as you bid out those projects and then longer-term what have you included in your assumptions? Thank you.

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

I think that is a very fair point that you make and really I sort of said it earlier, but it probably went by fast that when we think about this \$5 billion to \$6 billion over long periods of time to hold production flat, that is a real number. It is \$5 billion to \$6 billion today. If we have inflation and how that inflation comes back in depends on what's happened in the market and the industry, then the nominal number can go up over time. So it is \$5 billion to \$6 billion under today's conditions or low price conditions and in a scenario where we are moving back up to \$60s, \$70s, \$80s on oil price, that number is going to go up, it is going to reflate.

So we have done some estimates on how much of the cost reduction we've got. We think is structural versus cyclical but certainly there is a significant cyclical component that will come back as you move back up.

Now on some of these medium cycle projects the ones you mentioned, those costs are fairly well locked in already and so they are not going to change with reflation. The place where it will hit us first is in the unconventional North America just as that was the place where we first captured and most heavily capture deflation. I expect that is where we will see reflation coming back first.

So I also mentioned a minute ago that one of the things we have been doing to counteract that a bit is in the first quarter that is when we started to work on locking in pricing for longer periods of time particularly in the Lower 48 and the unconventional where we give up the right to be able to rebid when we think things are going lower and instead lock in the price as things move higher over a longer period of time. Just trying to delay when some of that reflation comes back into our numbers.

Edward Westlake - Credit Suisse - Analyst

Yes, a lot of folks trying to hedge oil prices but they should be trying to hedge costs right now probably.

Second question around APLNG, I mean this may just be low LNG prices, maybe startup costs but obviously the asset itself is performing well. But when I look at your earnings obviously everything got worse in Q1 but I thought you might do a little bit better in the quarter. Is there anything that we need to think about in terms of the startup costs or anything else around that asset?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Well, at APLNG, we are still heavy in the construction building Train 2. In fact we just finished all the final inlet air chilling etc. on Train 1 and now we are pushing 85 percent complete on Train 2 and still have a lot of construction work left to do this year. So there is still a lot of capital going into that so that is what is driving the continued capital injection into APLNG.

Once we've got the trains both running and you get into the 40s on crude price, say a mid-40s kind of price, then we will start to get cash back out from APLNG.

Operator

Paul Sankey, Wolfe Research.

Paul Sankey - Wolfe Research - Analyst

Good afternoon, everyone. Ryan, you presented at post-split, ConocoPhillips as having a differentiated model. It was somewhat inherited as a result of the split. As we go into this analyst meeting, what do you feel is going to be the differentiating aspect of ConocoPhillips that you want to promote? That is point one but question one.

And then maybe for Ryan or for AI, this time around it feels like we -- it may be different insofar as most companies are now saying they will be less likely to commit to very large high upfront costs, long-term projects and more likely to use the US unconventional to flex production. How do you think that makes things different when we begin as has been asked many times in this call when we think about how cost will inflate or not inflate going forward and how you can I guess differentiate yourself in that respect too? Thanks.

Ryan Lance - ConocoPhillips - Chairman and CEO

Thanks, Paul. I will take the first part and maybe AI can take the second part there.

I think so as we go into this analyst meeting, as I tried to say in my opening comments, Paul, I think sort of our disciplined capital approach is still fundamental. We had that at the spin and we will continue to talk about that. I think the portfolio differentiates itself and as we learn more about the unconventional, learn more the technology, the work that we have done over the last few years, we just see lower cost of supply and a lot more resilience in that portfolio. So I think the portfolio will continue to evolve and occupy a big piece of what we talked about.

And then certainly what is different is while the dividend decision was difficult, probably the most difficult I have had to make it has reset the company. So we have I think we have lowered the breakeven for the company and we start to generate free cash flow, which is something we didn't have at the spin as we came out of that. It was going to take until these major projects and we got through these long cycle time projects to get up and running before we reached that condition. That was the case post-spin and that is even more so the case now.

And I think what is different now is that a deeper and a better understanding of the low cost of supply that sits in the portfolio, it was captured which kind of informed our deepwater decision as well here about a year ago which was a tough one at the time. It looks better today obviously but was certainly a tougher one at the time. It has been informed by what -- as we have interrogated the portfolio and applied technology to that, what we can do with the existing captured resource base and the kind of growth we can see are flat capital for a decade or more just by exercising the options we have in the captured portfolio.

AI Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

I guess I would add to what Ryan said that one of the things we have seen as we have worked over the last few years to drive down the cost of supply across our whole resource base is that we have been differentially successful in doing that in our unconventional, our oil sands and even some of our legacy conventional versus deepwater. That is one of the things that has driven our thinking around deepwater is that we haven't been able to drive that cost of supply hasn't -- the structural part of it has been more difficult to drive it down versus say unconventional.

Now regarding your question on how industry comes back in the US on the unconventional side, I mean I don't think we are going to be the only ones thinking that we want to do some debt reduction before we go back to running rigs. So I expect that along with some of the effects we were

talking about earlier will cause things not to come back up at the same speed that they came down. And of course, there will be that delay effect as well just as we had on the way down, you will have that on the way up.

I already mentioned some of the things that we are doing on the supply chain side to try to manage our cost on the way up. But I will say we talked earlier as we get to a free cash flow position and we are judging whether we want to put some money to organic growth versus per share growth versus other uses of that capital, one of the things we will be looking at is what the cost is doing. If costs are reflating all the way back to where they were before, then our interest in putting that money back to work and that kind of work is going to be lower so we are going to be disciplined in managing those costs and the pace that we go back to work will partly depend, the attractiveness of that will partly depend, on how that reflation works.

Paul Sankey - *Wolfe Research - Analyst*

Great, thank you.

Operator

Scott Hanold, RBC Capital Markets.

Scott Hanold - *RBC Capital Markets - Analyst*

Thanks. I just got a couple of clarifications. First, you all obviously talked about the asset sales a little bit but just to clarify and when you say you have seen some softness in the market, is that specifically related to your deepwater package you have out for sale? And if I could add on to that question, AI, you obviously talked about the success in Senegal. Is Senegal, our presence in Senegal, still within the deepwater package of stuff you would look to sell?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

I mean we are seeing softness really across the board, Scott. We have said before we are just not going to fire sell anything and we are prepared to continue to appraise and develop if we need to. We still have some things on the market in Indonesia. We still have our deepwater portfolio in pieces on the market as well. So we are still trying to progress that but again, we know what our hold value is and we know what value it would take to sell the assets.

AI Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

With regard to Senegal, we have had a lot of success there finding a new play in the area and now we've drilled. We are on our fourth appraisal wells right now so we have drilled three appraisal wells, two drill stem tests now on our fourth appraisal well and we have clearly proved up high-quality reservoirs with good continuity across a large area. And so there has been quite a bit of interest in that asset and we will see what happens there. But we have to continue an appraisal program. It is going to take some more appraisal wells before that one is done but we will continue doing whatever appraisal work we need to do to establish the value of that asset.

Scott Hanold - *RBC Capital Markets - Analyst*

Understood. My follow up question, on the view of obviously focusing on more production per-share growth going forward, is there a situation you would envision where it doesn't make sense to maintain production and do share buybacks and obviously let your production base decline or is maintenance production sort of that minimum threshold and then you are going to look with free cash flow to buy back shares if it makes sense?



Ryan Lance - ConocoPhillips - Chairman and CEO

I think there may be periods of time where you don't put enough capital back in to maintain, but I think over time we want to maintain our production. We don't want to shrink and decline the production. There may be periods of time where some of that happens but over the long haul, no, I don't think we want to do that. We will be looking at what kind of maintenance capital it takes to hold our production flat.

Scott Hanold - RBC Capital Markets - Analyst

Okay, appreciate that. So it is not a shrink to grow type of mentality at all?

Ryan Lance - ConocoPhillips - Chairman and CEO

No, Scott, that is ex dispositions just to be clear. We do have some things in the portfolio that we still want to monetize over time but I think the size portfolio that we have we will be in the market doing some of that on a natural constant basis so all of my comments are ex disposition.

Scott Hanold - RBC Capital Markets - Analyst

Understood, thanks.

Operator

James Sullivan, Global Advisors.

James Sullivan - Alembic Global Advisors - Analyst

Good afternoon, guys. Thanks for squeezing me in. Just a couple of little cleanup things here. One is you guys loaded 11 APLNG cargoes during the quarter I think you said and a few more after. Do you have a number that were sold during the quarter?

Ryan Lance - ConocoPhillips - Chairman and CEO

All of them.

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

They were all FOB sales.

James Sullivan - Alembic Global Advisors - Analyst

So they are all taking title as they go on the ship?

Don Walleto, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

That is right.



James Sullivan - Alembic Global Advisors - Analyst

Okay, great. This is a little bit more out there but do you guys have -- and if you don't have the exact number just maybe what the trend is -- kind of up time percentage in the North Sea generally? I know you guys put a lot of iron up about two, three years ago over there. But just wanted to see obviously you guys are doing some infill work there and planning to but how has that trended over the last three years in terms of cost absorption and so on and using up that infrastructure?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

I thought I understood the question until the very end there. I thought you were asking about uptime.

James Sullivan - Alembic Global Advisors - Analyst

Uptime. Yes, I am thinking about uptime and the read through would then just be decreasing cost per unit by utilizing infrastructure.

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Okay. I see. I see. I get it. So we actually -- there is some opposing forces there. We have seen over that period of time in the North Sea an increasing uptime trend so we have actually been quite pleased with how our facilities have been running there and that has had an effect in lower unit costs. But we have also frankly have changed our philosophy a bit in the lower price environment where we are not willing to spend as much money to keep every barrel on as we were before and so that tends to ameliorate that trend a bit.

But still despite that change in philosophy, we still had an increasing trend and between that and our other deflation and other cost reduction efforts have seen a nice decreasing unit cost trend in those assets.

You may recall when we talked about deflation at our analyst day last year, we said it was going to happen first in the unconventional and it was because of the way we contracted, it would take longer to make its way to Europe and so we are seeing those supply chain benefits more this year rolling into our European operations that we weren't getting as much last year.

James Sullivan - Alembic Global Advisors - Analyst

Okay, great. So there actually might be a little bit of a nonlinear effect as the price comes up and you guys elect to increase uptime then?

Al Hirshberg - ConocoPhillips - EVP, Production, Drilling and Projects

Yes, if price gets up high enough where we are willing to spend those barrels, there is some potential for some nonlinearity there. I don't see that as a huge effect but yes, there is some.

James Sullivan - Alembic Global Advisors - Analyst

Okay, great. Thanks, guys.

Operator

Pavel Molchanov, Raymond James.



Pavel Molchanov - *Raymond James & Associates - Analyst*

Just one for me. This earnings season every company is being asked the same question, how are your capex decisions changing now that we are starting to see a more durable commodity recovery. You guys went in many ways kind of the opposite direction not just a cut but a sizable cut from February levels even though the curve was quite a bit higher. So what prompted another phase in this reduction against the grain of how the commodity has been moving?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

It is our decision to get out of deepwater. That is pretty much what drove the \$6.4 billion down to the \$5.7 billion, that was half of the reduction and then it is just really monitoring the business as close as we can and dialing it and not wanting to spend any cash to take on any more on the balance sheet. So we are going to defend the balance sheet and continue to wind down the deepwater program that we announced over a year ago.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Okay, but I guess the intensity of the wind down has obviously changed just in the last 60 days. So what prompted that?

Ryan Lance - *ConocoPhillips - Chairman and CEO*

The intensity of the wind down?

Pavel Molchanov - *Raymond James & Associates - Analyst*

Yes, so the pace at which you are cutting deepwater has shifted just since February.

Ryan Lance - *ConocoPhillips - Chairman and CEO*

We just made a decision not to drill the last couple of prospects with the Maersk Valiant drillship so that is sort of a kind of a cliff. That is not a wind down sort of scenario, we just got to the point where we just made a decision internally that we weren't going to drill the last couple of prospects so that was a fairly significant binary decision.

Al Hirshberg - *ConocoPhillips - EVP, Production, Drilling and Projects*

The more work we do on our portfolio improving cost of supply and all the other things I was talking about earlier, the less relative attractiveness the deepwater has for us in our portfolio. And so ultimately it is that sort of thing that drove us to say why are we going to drill these last two wells? We will save the money.

Operator

Asit Sen, CLSA.

Asit Sen - CLSA - Analyst

Thanks, good afternoon. I have two quick ones, one on cash margin and the second on Canada. If I'm looking at your Q1 2016 cash flow per barrel and compare it to potential incremental volumes coming on. So in other words, will the BOEs from Surmont, APLNG be accretive to the cash margin? How should we think about that because understand the benefit to the decline rate but on the cash accretion?

Second, on Canada, Al, I think you mentioned 6% increase in bitumen production so a decent shift in production mix. What does it do to the incremental cash flow profile in a very tough region?

Don Wallette, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

Well, I will try to address a question about the volumes coming out of the equity affiliates. So in this year at these prices and with the capital plans within those equity affiliates, we are actually making cash injections into the equity affiliates. We are not pulling cash out, there are no distributions. So from a margin standpoint, that is not going to be accretive to our consolidated margins.

Asit Sen - CLSA - Analyst

Got you.

Don Wallette, Jr. - ConocoPhillips - EVP, Finance, Commercial and CFO

And what was the second part of your question? (multiple speakers) Yes, that applies to bitumen and to LNG from APLNG.

Asit Sen - CLSA - Analyst

Okay, thank you so much.

Ellen DeSanctis - ConocoPhillips - VP, IR and Communications

Christine, I think that should wrap it up. Let's go ahead and thank people for your time and attention. By all means call us back if you have any thoughts or questions. Appreciate your attention and we will see you through the year and certainly on November 10. Thank you, everybody.

Operator

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

Editor

CAUTIONARY STATEMENT FOR THE PURPOSES OF THE "SAFE HARBOR" PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This news release contains forward-looking statements. Forward-looking statements relate to future events and anticipated results of operations, business strategies, and other aspects of our operations or operating results. In many cases you can identify forward-looking statements by terminology such as "anticipate," "estimate," "believe," "continue," "could," "intend," "may," "plan," "potential," "predict," "should," "will," "expect," "objective," "projection," "forecast," "goal," "guidance," "outlook," "effort," "target" and other similar words. However, the absence of these words does not mean that the statements are not forward-looking. Where, in any forward-looking statement, the company expresses an expectation or belief as to future results, such expectation or belief is expressed in good faith and believed to have a reasonable basis. However, there can be no assurance that such expectation or belief will result or be achieved. The actual results of operations can and will be affected by a variety of risks



and other matters including, but not limited to, changes in commodity prices; changes in expected levels of oil and gas reserves or production; operating hazards, drilling risks, unsuccessful exploratory activities; difficulties in developing new products and manufacturing processes; unexpected cost increases; international monetary conditions; potential liability for remedial actions under existing or future environmental regulations; potential liability resulting from pending or future litigation; limited access to capital or significantly higher cost of capital related to illiquidity or uncertainty in the domestic or international financial markets; and general domestic and international economic and political conditions; as well as changes in tax, environmental and other laws applicable to our business. Other factors that could cause actual results to differ materially from those described in the forward-looking statements include other economic, business, competitive and/or regulatory factors affecting our business generally as set forth in our filings with the Securities and Exchange Commission. Unless legally required, ConocoPhillips undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Use of Non-GAAP Financial Information - This news release includes the terms adjusted earnings, adjusted earnings per share and operating costs. These are non-GAAP financial measures. These terms are included to help facilitate comparisons of company operating performance across periods and with peer companies.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2016, Thomson Reuters. All Rights Reserved.

