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COP - ConocoPhillips Conference Call to Discuss 2016 Capital Budget and Operating Plan

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OVERVIEW:

On 12/10/15, COP announced its 2016 operating plan and expects 2016 capital budget of $7.7b.

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PRESENTATION

Operator

Welcome to the 2016 operating plan 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 & Communications, ConocoPhillips.

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

Thank you Christine and welcome to our listeners this morning. We're very pleased you joined us for this review of our ConocoPhillips 2016 operating plan. We're hosting this call and obviously providing a little bit more detail than usual for our capital release and we've included an agenda for this call that's found on page 2 of our slide deck.

Ryan Lance, our Chairman and CEO, will make some opening comments and really put the summary touches on our 2016 operating plan, again at kind of a high level. Matt Fox, our EVP of E&P, will then provide more of the details behind our plan. That will include some region reviews.

And Matt's also going to describe how our capital is being allocated this year and next. So we'll give you a tiny bit of a preview beyond this year.

Jeff Sheets, our EVP and CFO, will cover our financial priorities. Ryan will provide a few closing remarks and then we'll turn the call as usual over to our listeners for Q&A. During Q&A just to make sure everybody can participate and we make our way through the queue we are going to limit questions to one and a follow-up.

Our cautionary statement is shown on page 3. We will obviously be making some forward-looking statements this morning and our actual results could differ. The risks and uncertainties in our business are described in our periodic filings with the SEC and of course all that information is available on our website.

Now it's my pleasure to turn the call over to Ryan.

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Thank you, Ellen, and thank you all for joining us today. As Ellen mentioned this call represents a bit of a shift in our usual disclosure schedule. When we set the date for this call a couple of months ago we knew we could be announcing our 2016 operating plan against weak oil and gas prices and, well, we're certainly there now.

But despite uncertainty in the macro environment we think it's important to communicate our 2016 operating plan. We believe prices will eventually move higher but we don't know when, so we set a plan that balances short- and longer-term objectives for the business. We've retained flexibility to adjust if our outlook on the environment changes during the year.

Another reason to lay out our plan at this time is because it highlights the extent to which we've transformed ConocoPhillips, especially during this downturn. We are a very different company than we were just a couple of years ago. And I believe our plan will make this obvious.

So we're entering 2016 in a tough market but with a responsible plan. It's a plan that's underpinned by a lot of capital flexibility, a more competitive cost structure, a streamlined portfolio, a strong balance sheet and a low margin and low-cost of supply resource base.

If you move to slide 5 this gives you the punchline of what you'll hear today. Despite the tough market our dividend remains the highest priority use of our cash. We view the dividend level as a long-term decision and we've been in the current low price cycle for a relatively short period of time.

We're choosing to exercise flexibility during this downturn through capex and the balance sheet if necessary, not via the dividend. We're announcing a 2016 capital budget of $7.7 billion. That's $2.5 billion lower than 2015 capital guidance and more than $9 billion lower versus 2014.

In setting our budget we're flexing capital down appropriately for the price environment without losing opportunities or sacrificing the safety or integrity of our operations. Despite this very significant reduction in capital spending we still expect to grow production 1% to 3%. We could spend more capex and drive higher growth but I don't think that would make sense in this currently oversupplied market.

Our 2016 operating plan assumes operating costs of $7.7 billion. That's $0.5 billion lower than our 2015 guidance and $2 billion lower than 2014. Some of the most transformative work we've done in 2015 was around lowering our operating cost structure.

Under our plan we keep a strong balance sheet. We maintain an acceptable level of debt within our A credit rating, and non-core asset sales including the $2.3 billion we announced earlier today strengthens our cash position. And our plan closes the gap on cash flow neutrality.

Finally, while today's focus is on our 2016 operating plan we'll show you that our resource base provides multiple sources for profitable growth well beyond 2016. This will allow us to deliver our value proposition through the inevitable cycles to come.

And just to remind you that value proposition is shown on the next slide. This is the core of what we offer our investors, it drives our strategy. You see the elements of the value proposition we established when we launched as an independent E&P company.

It's a compelling dividend that provides an absolute return to our shareholders, disciplined growth with improved underlying margin and financial returns over time and financial strength via significant capital flexibility and a strong balance sheet. We understand our value proposition is being tested in the current price environment. However, we believe it's the right one for creating long-term shareholder value.

Now during 2015 we took multiple actions to protect our value proposition. These are described on the next slide. This slide shows a timeline of Brent prices since the downturn began in late 2014.

Superimposed on the plot are some of the actions we took in response to the downturn. We quickly cut our capex by reducing future and major project spending. We are high-grading our exploration activity and exercising flexibility in our conventional and unconventional drilling programs.

We moved quickly to capture deflation. In our development drilling programs we were in a unique position to do that because we have by design mostly short duration contracts in areas with significant flexibility.

We set a goal to reduce our operating costs, a goal that we have accelerated and far exceeded. And we've taken a hard look at our portfolio. It became clear that deepwater exploration and our non-core North American gas assets weren't going to compete for funding in the future, so we've taken steps to reduce capital and divest or transition out of some of those areas of the business.

And finally we raised the dividend. It was a modest increase but was an important signal to our owners and we continue to high-grade our portfolio. And that I'll describe on slide 8.

This slide represents the asset sales we announced this morning. We have line of sight to completing about $2.3 billion in assets sales including transactions that have already closed in 2015 or deals with definitive agreements in place that we expect to close later this month or in the first quarter of 2016.

About $600 million was completed as of the third quarter. About 45% of the proceeds were derived from nonproducing assets such as our interest in infrastructure assets in Europe and in Asia and a South Texas pipeline. The remaining 55% were derived from assets of producing properties primarily in North America.

These properties produced approximately 70,000 BOE per day in 2015, of which more than 80% was natural gas. These properties account for about 170 million BOE of reserves and would have generated about $125 million of cash flow in 2016 at current strip prices. So these assets will have minimal impact on our cash flows.

The left side of the chart shows our 2015 production guidance of 1,585 to 1,595 thousand BOE per day and that's consistent with the guidance we gave on the third-quarter call. The $2.3 billion of sale properties produced approximately 70,000 BOE per day in 2015. So adjusting for this our new same stores range is expected to be 1,515 to 1,525 thousand BOE per day.

That's the baseline from which the company expects to grow 1% to 3% in 2016. And we'll continue to high-grade our portfolio as part of our ongoing business.

Now let me jump to the next slide and show you the plan details. Here's the 2016 plan on a page.

Our capital spending budget of $7.7 billion represents a 55% reduction compared to 2014. The reductions come from completing several major projects, exercising flexibility, greater efficiency, deflation capture and project deferrals.

Now adjusted for the asset sales we expect to deliver 1% to 3% production growth and that represents a 3% CAGR since 2014. At the bottom of the chart we show the expected range of our 2016 production, which reflects the dispositions that I just discussed. Our operating cost budget of $7.7 billion represents a 20% reduction compared to 2014 and it also represents a 25% reduction in unit operating cost.

So this page highlights the transformation that we have undergone this past year. We're spending significantly less capital, we're delivering disciplined growth with improved underlying returns and margins via a much lower cost structure. We've made rapid changes in a rapidly changing environment and we believe we're well-positioned for the future.

So now let me turn it over to Matt. And he'll describe our plan in more detail.

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

Thanks, Ryan. I'll cover the capital cost and production drivers of the 2016 plan including some regional highlights. I'll conclude with some comments that address our outlook beyond 2016.

And what you will hear beginning on slide 11 is that we have a resilient plan with a lot of flexibility. Ryan's already covered the fact that our 2016 capital budget is set at $7.7 billion and this waterfall steps through the major sources of reductions starting from our 2014 level of over $17 billion. The first green brick represents over $2 billion of major project capital that rolled off between last year and this year, primarily at APLNG, Surmont, Malaysia and Europe.

Next we achieved over $3 billion of reductions from scope and efficiency improvements, mostly in the Lower 48, Canada and exploration. These reductions reflect activity cutbacks, project deferrals, infrastructure slowdowns and operating efficiencies.

Finally, this year we've achieved over $1 billion of improvement from deflation and market factors such as foreign exchange rates. That brings us to our estimate of $10.2 billion for 2015. This is down 40% from 2014 and more than 10% from our April 2015 guidance for the year.

As we move to 2016 we'll see another reduction in major project capex, mostly APLNG and Surmont. We'll continue to see some efficiency improvements in the Lower 48 that will drive a positive variance. And given current prices and the run rate effect going into next year we expect to see additional deflation and market benefits in 2016 as shown by the far right green brick.

So that's how we get to $7.7 billion capital budget in 2016, almost $4 billion lower than we projected in April. And we've noted on the far right that the $7.7 billion has about $800 million included for deepwater exploration and appraisal as we transition out of that program.

So on slide 12 I'll provide a quick update of our deflation capture efforts in 2015. From the start of the price downturn we responded quickly to capture deflation in both our capital and operating costs. We believe we were and are in the unique position to capture deflation because of our scope, supply chain approach and our global category management system.

So far in 2015 we've captured over $1 billion of deflation savings versus 2014. The left side of this slide shows how we've captured deflation across three big categories of capex in the Lower 48. In our stimulation services we had captured 10% versus 2014 in January, that expanded to 30% by March and we estimate we'll achieve about 40% in 2015 overall.

We've seen similar improvements in land rigs and cementing services to name a few. But we're not just capturing deflation across our capital spending or in the Lower 48. We're doing this all across the business.

And that's represented by the bars on the right side of this slide. Our deflation capture is diversified across our cost segments, our regions and by expenditure. In fact of the $1 billion of identified deflation capture we've achieved this year almost a third of it is operating cost, which brings me to slide 13.

This slide steps through the sources of our 25% improvement in operating cost per barrel since 2014, which goes right to margins. We've anchored this waterfall in 2014 adjusted actuals of $9.7 billion. In 2015 we had additional costs associated with our new production at Surmont 2, Gumusut, Lower 48 unconventionals, and a small increase for rig stack and subsidy costs associated with our West Africa rig.

We've reduced cost by almost $1 billion due to structural and efficiency improvements including headcount reductions and operational efficiencies. Almost $1 billion of additional deflation and market factor adjustments brings us to our 2015 estimate of $8.2 billion.

Moving to next year we'll continue to see production-driven cost increases as we add new production to offset decline and grow and the tail end of some rig subsidy costs. But these should be more than offset by the run rate impact of our 2015 reductions and further deflation. And that's how we get to $7.7 billion for 2016, $1 billion better than we expected back in April.

And of note the $7.7 billion includes about $400 million of deepwater operating costs which should roll off by 2017.

And if you turn to slide 14 I'll describe why we believe many of these savings will be sustainable, not just cyclical. We didn't just cut operating cost this year in response to lower oil and gas prices. We took the opportunity to examine how we do business.

The charge was this: lower our cost structure while preserving our value and our critical capabilities. In other words, make us the most competitive version of ourselves without elevating our risk.

This slide shows some of the organizational portfolio and optimization changes we've now implemented across the business. I won't cover all the points on the slide today. However, a few to highlight are we've reduced our employee headcount about 15% overall.

This includes some consolidation and reductions in management positions to streamline our decision-making. And the majority of these reductions were taken in our North American business unit and headquarters. We believe we now have an organization that's sized for a capital program that can flex up-and-down, albeit at a lower level than our previous plans assumed.

We also took a very hard look at our portfolio. You've seen the actions we've taken so far to discontinue investing in assets that don't compete in our portfolio such as deepwater and low-margin North American gas. We've slowed some development drilling activity mostly in the unconventionals, and major project spending at places like Surmont 3 in Canada and in Europe.

Finally, we're optimizing our center versus business unit capacity and capability. Our business units will run more autonomously and we'll maintain shared, specialized expertise at the center. We're focusing our technology efforts on challenges that we think can meaningfully lower our cost of supply and improve operating efficiency in the business.

We're standardizing and simplifying where it makes sense. These actions will make us a more competitive and focused company.

Our employees deserve a lot of credit for their efforts in this difficult but important piece of work.

Now I'll do a brief review of our regional plans for 2016 beginning on slide 15. Here is a world map showing our five producing regions. On the left are stacked bars of our 2015 and 2016 capex and production by region.

On the upper stacked bars you'll note that we're decreasing capex across every region. On the lower stacked bars you can see that we're growing volumes in three of our five regions, with Lower 48 and Europe showing slight declines.

In a nutshell, in Alaska our new projects and drilling activity can offset natural field decline. In the Lower 48, we're exercising our capital flexibility while staying prepared to ramp up or down if our outlook on prices changes. In Canada, ramp up at Surmont 2 will add to our low decline base of production.

Europe has contributions for project activity that will partially offset field declines. And in APME, startup of APLNG is underway adding to a strong base of production in the region.

The red dots indicate the places we will have exploration activity during 2016. It's actually quite an active year for us as we fulfill our exploration commitments on our high-graded prospects.

Now let's do a quick tour of the regions beginning on slide 16. The theme in the Lower 48 is to maintain our operating momentum, continue to capture efficiencies and deflation but be prepared to exercise flexibility as needed. In the upper left corner of the slide we've included a chart of recent third-party data that shows ConocoPhillips still has the lowest wellhead breakeven among companies greater than $5 billion of market cap.

We have a world-class inventory of projects here but we're choosing to drill at a measured pace in these plays. We're still benefiting from our technology learning curve and we don't lose these opportunities by deferring them until prices improve.

The plan assumes we'll spend about $2 billion in the unconventionals with a rig count of 13. That's six in the Eagle Ford, four in the Bakken and three between the Permian unconventional and conventional plays.

This is the same number of rigs we've been running in the Lower 48 since June. However, as I just described, we have the option to flex up or down as conditions change.

We expect to reduce Lower 48 capital by about 30% and see a production drop of about 3%. The capital reduction is driven primarily by deflation and lower infrastructure spending but also by greater efficiencies in the unconventionals. For example, we've reduced drilling days per well by about 25% versus last year in the Eagle Ford and Bakken.

Finally, we'll spend about $450 million of capital in the deepwater Gulf of Mexico. And there'll be more on that later.

If we turn to 17 for a quick review of our Canada segment. In Canada our 2016 capital will be down about 30% compared to 2015, but volumes are expected to grow by about 10% year over year.

The story here is the ramp up of Surmont 2 where we're making great progress and hitting all of our milestones. Additional phases of FCCL are also expected to start up in 2016.

We continue to make strong progress in our technology efforts in the oil sands. We have a natural advantage given our top-tier geology, but we're enhancing that advantage with some innovative work to lower our cost of supply in this very large resource position and drive down greenhouse gas emissions.

We don't have much capital allocated to the Canadian unconventionals in 2016, but we retain our option on this vast liquids-rich position. You'll notice we also have about 20% of our 2016 capital allocated to exploration and this is primarily for two wildcat wells offshore Nova Scotia, the first of which is currently drilling.

Next I'll cover our Alaska segment on slide 18. In Alaska, capital is expected to be down slightly year over year, but with volume growth. And that's a credit to recent projects startups of CD5 and Drill Site 2S and ongoing development drilling at Prudhoe and Kuparuk.

We recently sanctioned the GMT-1 project on the Western North Slope and we'll continue to pursue step-out exploration around existing infrastructure. Over the past couple of years we've been able to change the profile of our Alaska business. We've transformed a declining production base into one that can deliver stable production for a decade. Finally, we're continuing to participate in commercial and pre-FEED activity for AKLNG.

Next I'll review Europe on slide 19. We continue to make strong progress across the European assets on lowering cost and improving efficiencies. Capital spending in Europe will decline in 2016 versus 2015 by about 15%, which will result in a decline in production.

Some of this decline is due to the fact that we'll have significant turnarounds in 2016 at both Ekofisk and J-Area.

Despite prudently deferring some of our major projects in Norway and deferring development drilling in J-Area we continue to invest in several high-return programs such as our development drilling campaign at Ekofisk and Eldfisk. These programs take advantage of the new infrastructure we've installed over the last few years. We're also proceeding with our project investments at Alder, which is expected to start up in the second half of 2016 as well as Clair Ridge and Aasta Hansteen.

Now I will review the Asia Pacific and Middle East segment on slide 20. APME in a nutshell, about 30% lower capex with about 10% higher volumes. The big driver in APME for 2016 is a startup and ramp of APLNG.

We've started up the plant and we've just begun to make LNG. We're on track to load our first LNG cargo in the next few weeks. We'll see a significant reduction in capital in our APME segment in 2016.

We expect to spend about $600 million at APLNG next year. This is a larger contribution to APLNG than we've previously anticipated, primarily due to catch up for 2015 deferrals and lower anticipated LNG prices. We'll carryout some development drilling around our legacy positions and continue projects in Malaysia and China.

These projects such as Malikai and Bohai Bay are high-return investments that will keep APME growing for the next several years.

Next I'll quickly discuss the transition year we have planned for deepwater exploration and appraisal in 2016 and that's shown on slide 21. As we previously announced, we plan to implement a phased exit of deepwater exploration. Our 2016 activity will focus on three areas: Eastern Canada, the Gulf of Mexico and Senegal.

In the Gulf of Mexico we continue to high-grade our prospect list. We recently spud the Melmar well. This is the first of three planned operated exploration wells, which will be followed by Horus and Socorro.

An exploratory well is currently drilling in the Gibson prospect and the Keathley Canyon area and appraisal activity will continue at the Gila, Shenandoah and Tiber discoveries during 2016. We're also currently underway in a six well exploration and appraisal program in Senegal. Lastly, we're currently drilling in Nova Scotia on the Cheshire well and a second exploration well is planned for 2016.

So 2016 is actually an active year for our deepwater exploration program as we pursue a phased exit. We don't expect to spend capital in these programs in future years and that represents about $800 million of future capital flexibility. And that flexibility is at the core of our strategy to create value beyond 2016.

We'll do that by developing our captured, diverse, flexible low cost of supply resource base which is shown on slide 22. We described our 44 billion barrel resource base at our Analyst Meeting in April. Over 24 billion barrels of this resource has a cost of supply of less than $75 a barrel Brent equivalent and 16 billion barrels has less than a $60 a barrel cost of supply.

That alone represents almost 30 years' worth of current production at less than $60 a barrel. The chart shown is based on mid-year 2014 estimates, so the cost of supply doesn't reflect deflation or technology improvements and we're in the process of updating our resource assessments and cost of supply for these factors. But it should be clear that this captured resource base will allow us to deliver profitable organic growth well beyond 2016.

If you turn to slide 23 I'll give you a preview of how we expect to allocate capital across this resource base over the next two years. The bars on the right side of this chart describe how we expect to allocate capital in 2016 and 2017 across several diverse categories. We believe diversification is an important feature of our strategy.

The left bar shows how we would allocate this capital between our growth engines. The majority of our capital is going to go to conventional and low cost of supply unconventional investments, reflecting the fact that our megaprojects in the oil sands and LNG are largely behind us. Regionally about two-thirds of the capital is allocated to North America.

The third bar is telling. Under this plan about 30% is earmarked for flexible programs. That means we retain the ability to reduce capital in lower price environments but also means we can flex up in higher prices.

About 20% of our capital is planned for base maintenance because we are not going to compromise the integrity of our assets in a low price environment. And we're going to continue to direct some capital to projects that provide step function medium- and longer-term growth because we think the balance of long and short cycle projects is important.

And finally, the bar on the far right shows our capital plan split by cost of supply. Almost 85% of our capital is targeting resources with the cost of supply below $50 a barrel Brent equivalent. This includes our core unconventionals as well as opportunities across our conventional legacy fields, another advantage of diversification.

Over the next two years almost 100% will be invested, directed to investments with lower than a $60 cost of supply. And the capital targeted to above $50 a barrel represents longer cycle time projects that we expect will improve to a lower cost of supply over time.

This is our strategy on a page. We'll allocate capital across a diverse, flexible and low cost of supply resource base to deliver a compelling dividend and profitable organic growth. We believe this plan is quite unique among E&Ps.

So that wraps up our capital and operating plans. Jeff will now provide a financial update.

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

Thanks, Matt. I plan to cover our financial priorities and plans for 2016 and beyond. As you can see our financial priorities are listed on slide 25.

Our top priority is the dividend. As Ryan mentioned the compelling dividend is a core element of our value proposition and we think it is still appropriate. We're continuing to drive positive momentum in our underlying financial returns, a key focus area for us especially in this low price environment.

You've heard a lot about how we're lowering our cost structure and starting up several major projects. We have a priority to maintain a strong balance sheet which allows us to continue to manage through market volatility. And our ongoing asset sales provide additional financial flexibility to weather the cycles.

We are rapidly closing the gap on cash flow neutrality. Our goal is to get to sustainable cash flow neutrality in 2017. The actions we've taken this year will make it easier to achieve this across a range of prices.

These priorities aren't new. They are really the same ones we've had since the spin. They've been tested in this year of low prices but we believe they are the right ones for a company of our size and maturity.

I will make a few comments about each of these in more detail beginning on the next slide. Our value proposition is not just about growth. We've maintained a consistent focus on margins and returns.

Our portfolio, our cost structure and our operating flexibility have been transformed. We're on a path to reduce unit operating costs by 25% and we're high-grading our portfolio by exiting or selling assets that won't compete for funding.

Over the next several years we expect underlying returns to improve by a couple hundred basis points or more and that's without higher prices. Returns will benefit from substantially lower operating costs that Matt and Ryan have already discussed.

An era of big major project spending is behind us with major project startups in the oil sands and APLNG making a difference. As the chart on the lower right shows these assets comprise about 30% of our average capital employed. After years of investments these projects will begin contributing to profitability and become a source of cash, not a use.

As you saw from Matt's capital allocation slide a higher percentage of our future capital will be directed to shorter-cycle, higher-return investments from a captured low cost of supply resource base. So we're addressing returns in several sustainable ways which should continue to increment up our financial returns over time.

On slide 27 I'll make a few comments about our balance sheet. Balance sheets like ours are made for times like these. In a cyclical business it's an advantage to be large and diversified and to have a strong balance sheet with access to liquidity and capacity to weather the downturns.

Across the top of this slide you'll see three categories of business risk profiles as assessed by Standard & Poors. On the left with the strongest profiles are ConocoPhillips and the integrated oil companies. Companies with higher-quality business risk profiles have capacity for higher leverage ratios within the same credit rating than companies with lower profiles.

We're rated single A by S&P and Fitch and an A2 by Moody's based on our IOC-like size and diversification. We've included a couple of recent quotes from Moody's and S&P which illustrate this point.

Under our current 2016 operating plan we would expect to have modest cash flow shortfalls that we would manage by utilizing our cash balance, generating additional proceeds from non-core asset sales and issuing some debt if needed. We believe we have ample capacity to manage through this cycle without going below an A rating.

Next I want to talk about our path to sustained cash flow neutrality on slide 28. This slide highlights the levers we have at our disposal and the actions we can take to close the gap on cash flow neutrality. Ryan and Matt have already outlined many of these actions for 2016.

We will flex our capital of $7.7 billion. We will lower our operating costs to $7.7 billion. We'll get production growth from the startup of major projects and we would expect to achieve additional non-core asset sales.

When we add all that up if we see another year in 2016 like we've seen in 2015 we would expect to have modest borrowings, say about $2 billion, which is well within a single A credit rating. As we go into 2016 we have additional flexibility and momentum that will help close the gap. And by 2017 we would expect to get some help from somewhat stronger prices.

In 2017 additional capital associated with APLNG and the deepwater rolls off creating over $1 billion of additional capital flexibility. Where we direct that capital will depend on our market outlook at the time. We will maintain our diligence on operating costs.

In addition costs associated with the deepwater transition should also begin to come down. The cash flows should improve due to high-margin liquids growth from our major projects. And as prices improve our cash flows will get an added boost from the usage of tax losses that we've accrued during periods of low prices, which create significant near-term leverage to price recovery.

We would also expect to have some additional non-core asset sales in 2017. Based on these assumptions we would not expect to require additional borrowings in 2017 while maintaining our A credit rating.

But what if prices in 2016 turn out to be much different than we have assumed? I will cover that on slide 29. We understand our asset base, our cost structure and our performance drivers very well.

But we don't know with certainty where prices are headed. In developing our 2016 plans we've assumed that on average we will see a price environment in 2016 that's much like 2015. However, if we believed average prices were going to be significantly different, say $10 a barrel higher or lower than 2015 average prices, you could expect us to take some measured actions.

On a lower price side we would expect to capture additional deflation and realize further efficiencies. We have flexible discretionary capital in our 2016 plan that we can choose to reduce.

We would expect lower production growth but that would probably be a sound decision in a lower price world. We would use some of our balance sheet capacity. This would be a tough environment but we have the flexibility and scale to take these steps if prices are meaningfully lower.

On the higher-price side we have the option to increase capital in our most flexible programs, which would bring additional production and cash flows. We would maintain our focus on operating costs. We would take the opportunity to strengthen our balance sheet, which is why we would be disciplined in the degree to which we increase investment capital.

But across this range of prices our priorities are consistent. We pay our dividend, focus on organic growth while flexing capital as needed, improve underlying margins and returns, keep our balance sheet strong, continuously high-grade the portfolio and, finally, get to cash flow neutrality and stay there through the cycles.

Now I will turn the call over to Ryan for some closing comments.

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Thanks, Jeff. So before we go to Q&A let me make some quick summarizing comments if you'll turn to the next slide. Today we presented our 2016 operating plan.

Underlying this plan is the significant transformation we've made as a Company over the past few years which we've certainly accelerated during 2015. As we've said all year we're prepared for an environment in which mid-cycle prices will be lower and more volatile than in years past. Consistent with that view we've moved quickly to create the portfolio and strategy characteristics that we believe are needed to win in this new world and they are listed here.

The winners will have a diverse, low decline base of production. This underpins a stable cash flow stream that in our case will sustain our dividend. Companies with a large, captured, low cost of supply resource base have options and choices for capital allocation.

In our case we can fund years of profitable organic production growth from what we have in our captured inventory. It's important to have a portfolio of flexible, short-cycle options. Ours is unique among large companies.

This allows us to scale up or down our capex and growth rate in response to price. That said we also believe the business will continue to need medium- and longer-term cycle investments. In our case these projects provide periodic step function production increases and add to our low decline base.

It's critical to sustain a low cost structure. In 2015 we didn't cut costs just to conserve. We took the opportunity to reset our cost structure and our ways of doing business to be more resilient.

We've said it many times: a strong balance sheet is an asset, which gives us the ability to withstand the cycles. Finally, we think it's important to return capital to our shareholders. While a dividend is not flexible like capital or cost it's an important part of attracting and retaining a high-quality shareholder base.

It provides a real return to our owners during every part of the cycle and it instills important discipline in how we allocate our capital. This list describes ConocoPhillips. We've taken actions to establish and build upon these characteristics.

We don't have a crystal ball to predict where prices are going. But we have the next best thing, a set of characteristics that we believe work across a broad range of price scenarios. We also believe they are unique among E&Ps.

So in closing here's a recap of what you've heard on slide 32. We continue to believe it's important to pay our shareholders first. We've set a $7.7 billion capital budget that delivers growth.

We're guiding operating costs to $7.7 billion. We maintain a strong balance sheet and are closing the gap on cash flow neutrality. We believe we've set a reasonable balanced plan, and one that retains flexibility, a key in this environment.

Now looking ahead we have a resource base that can deliver growth well beyond 2016. It's already captured, it's diverse and it has a low cost of supply.

We have what we need to deliver our value proposition. So as always we look forward to updating you as we go through the year in 2016.

So with that, let me turn it back over to the operator and we'll take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Blake Fernandez, Howard Weil.

Blake Fernandez - *Scotia Howard Weil - Analyst*

Folks, good morning. I appreciate the details in the presentation.

First question was on deepwater. I was hoping you could remind us of what if any booked reserves and production you may have there and maybe just an update on the process to potentially exit.

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

So Blake, we don't have any reserves booked associated with the deepwater assets that we're divesting. These are exploration assets. Some are in appraisal but we don't have reserves booked yet because the projects are not approved.

The process that we're in we're running in basically two phases. We have a phase where we're engaging potential buyers that might be interested in buying the full package and then we anticipate perhaps moving to a second phase where we sell the package as individual elements. So we're really in the early stages of that process just now.

Blake Fernandez - *Scotia Howard Weil - Analyst*

Okay thanks, Matt. The second question was on the capital. Jeff I think mentioned that there's about $1 billion of additional flexibility going into next year.

I was hoping to clarify. I think there was a comment of about $600 million of APLNG, I'm just trying to understand the moving parts of that $1 billion.

Does that include exploration, which kind of rolls off? Just some clarity on that would be appreciated.

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

I will take that one, Blake. Yes we have about $800 million going into the deepwater. We wouldn't expect to be spending that next year and about $600 million going into APLNG.

So we wouldn't expect to be spending that. So you can regard that as additional flexibility that we could choose to reallocate that capital to something else or we could choose to run capital at a lower level in 2017. That's a choice we don't have to make until I guess this time next year.

Blake Fernandez - *Scotia Howard Weil - Analyst*

Matt, just to be clear, though, that would put you above the $1 billion of flexibility mentioned previously, right?

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

That's right.

Blake Fernandez - *Scotia Howard Weil - Analyst*

Okay, thanks a lot. I appreciate it.

Operator

Doug Leggate, Bank of America. Please go ahead.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Thanks, good morning everybody. Guys, I wonder if I could do kind of a follow-up to Blake's question. I guess what everyone is really trying to figure out especially given your unique dividend situation is just what your ultimate kind of capital flexibility or that horrible phrase breakeven capex would look like?

And I wonder if I could just ask you to revisit for us where you would see a level where you can hold production flat I guess theoretically, fund the dividend, and how you would think about allocating capital incrementally in the event of a recovery. And what's behind my question is the $1.4 billion that you just laid out, but there's also $600 million of operating cost that goes away with the deepwater as well, I'm guessing.

So all things considered, it would seem that your $60 breakeven probably has some downside risk to it. So if you could help us with that, and I've got a quick follow-up, please.

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

So Doug, there's about $400 million of operating costs associated with the deepwater, not $600 million. So $7.7 billion minus that $1.4 billion that we mentioned would take you close to $6 billion. Coincidentally, that's about the level of capital that we would need to spend to maintain flat production from 2016 and beyond and then for several years.

So we could choose to take the capital to that level if we wanted to, and then maintain flat production. So that's a choice, again, that we'll face as we get to this stage next year, but it's definitely a good flexibility to have to be able to maintain production at those levels for a $6 billion capital budget.

Doug Leggate - *BofA Merrill Lynch - Analyst*

So if you put the dividend onto that -- maybe it's a question for Jeff but -- I guess I'll make this my second one because I don't want to hog the call. But if you stick the dividend on top then, what do you think the commodity deck looks like in order to be able to meet your obligations?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

That's probably around a $60 Brent price, Doug. Of course that depends on what's going on with the rest of the commodities as well. But a $60 Brent environment would fund the capital that we think we would need to maintain flat production and the dividend.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Before disposals, Jeff, I'm assuming?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

Yes on a cash flow -- that would be a cash flow neutrality point for the next several years with $60 Brent funding the capital that needs to have flat production and the dividend. We will probably continue to have disposals as we go along like we've said for some time that could provide additional flexibility for us.

Doug Leggate - *BofA Merrill Lynch - Analyst*

All right. I will leave it there. Thanks, guys.

Operator

Doug Terreson, Evercore ISI.

Doug Terreson - *Evercore ISI Group - Analyst*

Good morning everybody. Ryan, the downturn is obviously still underway and you guys have adjusted in pretty prompt fashion along the way. But in an environment whereby there is a recovery in the oil market and prices rise in 2016, which I think was one of Jeff's scenarios, what if any changes and over what period of time are changes likely for the company's spending plan?

Let's just say that Brent were to return to $60 for a six- to nine-month period for instance, would higher spending follow in fairly prompt fashion or would enhanced financial flexibility be higher priority? So if you could comment on how you're thinking about your response time and any obstacles to responding that the company and/or the industry may face and then how you're balancing these factors I would appreciate it.

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Yes, thanks, Doug. I think we're trying to balance all those pieces as we go through this cycle and see some recovery coming out the other end of it.

As I've said, we've said repeatedly the balance sheet will compete for capital just like capital will that we reinvest back in the business. So I think first order of business and we've said this we'll use the balance sheet on the downside as we fund our programs and create the flexibility we've got in the portfolio. And we're prepared to repair that on the upside.

So I would say as we see sustainable longer-term higher prices we'll fix the balance sheet and then we'll put more capital into our flexible programs that provide growth. And the amount of growth will be a function of the absolute capital that we're reinvesting in.

But as Matt went through, we've got a lot of low cost of supply opportunities to invest in. So, but the balance sheet will be important to get that into a position because we think we're in a world of more volatile prices and we've got to be prepared for another downturn depending on how quickly this cycle ramps back up.

And the lower we go for longer the upcycle will come and it will be rapid. So we have to be prepared for another down cycle on the other end of that. So the balance sheet is important for us to maintain that flexibility.

Doug Terreson - *Evercore ISI Group - Analyst*

Ryan, are there any obstacles that you're thinking about or that you've experienced in the past that the industry may face when you do decide to respond? Meaning after balance sheets are rehabilitated, anything you guys are thinking about these days that could emerge?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Well, not beyond the part that does, some of the service side will come back, we'll see some inflationary pressures but I think we're well prepared to manage that with some of the changes that we've made in how we're operating the business. And we're prepared just to ramp up our own business in the captured resource base that we have. I don't see anything unique coming out of that, it's just positioning the company to be able to respond to something that we think is a longer-term recovery and higher prices.

So that's the beauty of the portfolio that we've created, we've got that flexibility to ramp up or ramp down depending on the markers we see. We're going to be tracking all of those, inventory levels, supply/demand, everything that everybody is watching and then with a sharp eye and focus on the cost side.

Doug Terreson - *Evercore ISI Group - Analyst*

Great, thanks a lot.

Operator

Phil Gresh, JPMorgan.

Phil Gresh - *JPMorgan - Analyst*

Hey, good morning. First question I guess is just a follow-up on the repairing of the balance sheet priority in the higher price environment. I was just curious if there's a specific level do you think it would be appropriate to get to to handle a more volatile price whether it's on an absolute level or a ratio basis, just generally how you're thinking about it today?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

Generally, we feel like it's important to have a strong investment-grade credit rating. We've talked about it being a single A credit rating. We think there's a lot of capacity left still in that rating to handle the downside prices.

I think a lot of it back to the previous question on how much does incremental cash flow from higher prices go to the balance sheet will depend somewhat on how long of a period of low prices we've gone through before that happens. We are not uncomfortable with the level of debt that we have on our balance sheet currently. So if we don't go beyond adding to the current balance sheet debt levels then we probably don't have a feeling that we'll need to try to strengthen it beyond that point.

But if we end up going to a prolonged period of lower prices and we add to our current balance sheet debt levels we'll probably want to bring them back to the kind of strength that we have today.

Phil Gresh - *JPMorgan - Analyst*

Okay, got it. And then you mentioned some additional flex capital you might have in 2016 in a lower price environment and you also actually did not mention in a lower price environment additional asset sales.

So I was just curious how we should think about what additional flexibility you actually see for 2016 capital? And if that was purposely mentioned that you wouldn't want to target additional asset sales and if the priority is really just the $1 billion to $2 billion additional over the next two years?

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

If you look at the last slide on my deck there that shows the capital allocation you can see that about 30% of the capital that we're expecting to spend remains flexible. So we do have the option to reduce capital if we choose to.

We still plan to and we have assets on the market, the deepwater assets and our Block B assets in Indonesia are ones that people are aware of that are on the market. So we would expect to see some proceeds from dispositions in 2016 in addition to the proceeds that we announced this year. So flexibility in the capital, some additional asset sales and if there's a requirement to make up a difference then we will use the balance sheet to do that.

Phil Gresh - *JPMorgan - Analyst*

And just to clarify you're saying 30% flexibility specifically in 2016?

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

Correct.

Phil Gresh - *JPMorgan - Analyst*

Okay, thank you.

Operator

Paul Cheng, Barclays.

Paul Cheng - *Barclays Capital - Analyst*

Hey guys, good morning. Jeff, I don't think that you would need it but can you tell us what is your estimate of the total debt you can raise before you would drop to a BBB?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

I don't know that we can put an exact fine point on that number, Paul. That's really kind of the rating agencies' call there.

We have that we will just continue to talk about it is we have capacity to work our way through 2016 and before we in a lot of different price scenarios and still maintain the single A credit rating.

Paul Cheng - *Barclays Capital - Analyst*

Okay, the second question is that Matt, when you're looking at your opex reduction and all that, comparing to I guess comparing to the third-quarter or the fourth-quarter operating cost level, are we seeing a significant incremental drop that you expect next year or that this is sort of like getting the full-year benefit and not incremental benefit? And incrementally is there any particular area you're going to see the most efficiency gain or the cost reduction from the current level?

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

So we wouldn't expect it to be operating cost to be as high as they were the third quarter. A lot of the actions we took specifically on our headcount happened at the beginning of the fourth quarter or during the fourth quarter.

So we're going to benefit from the run rate for the full-year and we're going to benefit from reductions that are specifically going to occur during the fourth quarter. So it's a mixture of both, Paul.

Paul Cheng - *Barclays Capital - Analyst*

I see. How about efficiency gain? Any particular area you're going to see the most potential for the next one or two years?

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

We're still seeing very strong efficiency gains in our unconventional position. Are you talking, Paul, about operating cost or about capital cost?

Paul Cheng - *Barclays Capital - Analyst*

Both.

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

Yes, so we're seeing a lot of capital cost efficiencies in the unconventionals. In fact, we're seeing it across our whole business and the same really applies to operating cost.

We're in a price environment where it makes sense to question every bit of operating cost that you spend to make sure you're getting value for that operating cost. And so that results in value efficiencies and the operating cost as well. So basically across the board we're seeing efficiencies that are helping both on the capital and the opex side.

Paul Cheng - *Barclays Capital - Analyst*

Thank you.

Operator

Guy Baber, Simmons & Company.

Guy Baber - *Simmons - Analyst*

Good morning everybody and thanks for all the detail and for hosting the call. It's very helpful in a volatile environment.

My first question was with the phased exit from deepwater exploration and lower exploration spending in general, in the type of spending environment you've discussed can you just discuss the outlook for portfolio and resource base renewal and replenishment through the cycle? Given you have a sizable portfolio is the US unconventional base and position significant to support renewal for the entire company, do acquisitions eventually play a bigger role or does that signal a need to perhaps shrink further? Just trying to understand the strategy and the thought process behind replacing and replenishing the portfolio.

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

Yes, so our long-term growth will come from a few different sources. Clearly the conversion of our resource base, some of that challenged resource base that we show on the pie chart to unchallenging that, reducing the cost of supply of the existing resource base that's less than $75. That's going to get to a lower cost of supply as well.

So a lot of the long-term growth can come from within the existing captured resource base. But we are an E&P company and we've got strong capabilities in exploration. So that will also contribute over the long term to replenishing the resource base and delivering growth.

Now we have removed deepwater as an engine for that exploration resource addition but we still have significant opportunities in the unconventionals both in North America and internationally. And we have a very strong portfolio of near infrastructure options in the conventional area in places like Alaska and Europe and elsewhere. So we're going to be providing additional resource growth from both of those areas.

Guy Baber - *Simmons - Analyst*

Okay great. Thanks, Matt.

And my follow-up was can you just discuss the decision process behind deciding to maintain your US rig count flattish at current levels at 13 rigs with the forward curve right now at $43 WTI in 2016? Is that reflective of a desire to maintain capability in those plays, is it just demonstrative of your confidence in the efficiency gains which you've captured or just overall comfort in the overall level of spend? And could you discuss also along with that if you have any update with respect to the trajectory expected for your US unconventional production with the 13 rig count?

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

Yes, so the answer really is you sort of answered your own question because it's a mixture of all of those things. When we were setting the capital program for the unconventionals we were trying to balance the short-term, medium-term and long-term characteristics there.

We've got very strong operating momentum, just now. We've got good rigs, we've got good crews and we've got very good wells to drill that are economic at current prices. So with that on one hand and then we want to use, are willing to use the balance sheet, but we don't want to overuse the balance sheet. So that's the sort of short-term view.

In the medium term we will have a modest decline that's about 3% decline in the unconventionals. But we really want to maintain a strong base so that we can grow when prices recover. We don't want to let that base fall away from us too far.

So this is our medium-term view. And then in the longer term we want to continue to learn from our pilot tests and we want to continue to capture the efficiency gains so that when the recovery comes and we ramp up production we're doing that in the most efficient way possible and maximizing the value of the resource base that we have. So it's a mixture of all of those things.

And deferring some of this production isn't really a problem because we're not losing any of the resource base by doing that. So those were the sort of things we're working on reminding me to decide to enter the year with the same number of rigs that we been running for most of this year.

Guy Baber - *Simmons - Analyst*

Very helpful, Matt. Thanks for the comments.

Operator

Paul Sankey, Wolfe Research.

Paul Sankey - *Wolfe Research - Analyst*

Hi, good morning everybody. Thank you for your excellent disclosure. It's greatly appreciated.

I had a couple of questions, a bit of specifics. I will start with a follow-up to the previous.

You said that your US rig efficiency is from 2014 to 2016 is a 25% gain. Could you give us a sense for the 2015 to 2016 progression just because we're trying to get to a bit more specific performance improvements year over year? Thanks.

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

Time will tell on that, Paul, of course but we do expect to see some continued efficiency gains as we move into the year. Probably of the order of 10% would be a reasonable expectation if you're trying to get some sort of calibration. But so we do expect this to continue to see efficiency gains.

We are running the best rigs with the best crews and we are focused on achieving those efficiency gains and our guys are doing that every day. So we will see continued improvement.

Paul Sankey - *Wolfe Research - Analyst*

Thanks, Matt. So basically you're saying that the 25% is mostly achieved in 2015 and then there's a further 10% to come? Or that we've seen 15% in 2015 and we will see another 10% and 2016?

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

The former.

Paul Sankey - *Wolfe Research - Analyst*

Okay, so the majority of the 25% has already been achieved and there's some potential for some more but at the moment you're sticking with a 25% gain from 2015 to 2016 to be safe.

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

The 25% gain is already realized and we expect to see additional gains as we go ahead.

Paul Sankey - *Wolfe Research - Analyst*

That answers the question. Thank you. On Alaska I guess one of the perceptions of ConocoPhillips is that you've got a couple of major areas that are very mature.

It's notable in the case of Alaska that you're succeeding actually I think here in raising volumes with flat capex. What changed there? It's being perceived obviously to be a decline area.

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

We've been developing opportunities in the for example in the Western North Slope from our CD5 opportunity. And we just approved the GMT-1 project and we have opportunities to move to GMT-2 in the Western North Slope.

We've been having great success in Kuparuk for example with our coiled tubing drilling program. We're actually bringing in a new dedicated coiled tubing drilling rig to Kuparuk. It's really a testament to the ingenuity and the technology deployment and some exploration success in Alaska that allows us to give us a slight increase in production next year for less capital and we believe that we can sustain that for 10 years.

It was also helped to some extent by the change in the fiscal regime that the government made the SB 21, which sounds like old news now. But that did put an environment in place that gave us encouragement to ramp up our capital.

Paul Sankey - *Wolfe Research - Analyst*

Got it. And then the obvious continuation is the North Sea you have got declines but could you clarify the turnaround?

I think you said it's a heavy turnaround year. How much of the volume decline is a one-off and how much is just the secular?

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

I think it's some 5,000 barrels a day associated with the triennial turnarounds in the Central North Sea at the Greater Ekofisk area and the J-Area. So every three years we take those facilities down and this is one of those years that's coming up. So that's about the incremental downtime that we'd expect to see.

(multiple speakers)

Ellen was just reminding me that will all be seen in the second and third quarter of next year.

Paul Sankey - *Wolfe Research - Analyst*

And keeping the same guidance how has the fiscal regime changed things there for you?

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

I think the UK government would be advised to make additional changes to the fiscal regime. The changes that they made so far are helpful. They could do more and they should do more if they want to keep a North Sea business going in the UK.

Paul Sankey - *Wolfe Research - Analyst*

Yes, would it be a disposal candidate?

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

It's not something that we're currently including in our plans to dispose of the UK.

Paul Sankey - *Wolfe Research - Analyst*

Great, thank you all.

Operator

Edward Westlake, Credit Suisse.

Edward Westlake - *Credit Suisse - Analyst*

Yes, good morning and again I echo the thanks, great presentation and color so far. Just again coming down to production sustainability and I guess this is beyond 2017, you did a big presentation in March where you laid out how much resource you had in conventional, Alaska, shale. Can you just give us a sense of the mix of I guess production that would offset decline post-2017?

How much is going to be shale? How much is going to be in the conventional base shorter cycle stuff to keep the capex at that low level and yet still maintain production?

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

You're saying to maintain production flat, so the comment we made earlier about $6 billion of capital required to maintain it flat? The capital split associated with that is actually quite similar to what you see on the chart that we showed at the end of my presentation. It's page 23 of the chart.

So it would be maintaining a similar profile, maybe actually a bit less in the unconventionals in that profile if we only wanted to maintain flat production because a lot of the sources of growth that are in the portfolio beyond 2017 can come from the unconventionals. But that would give you a sense of what it would look like beyond 2017 if we decided to that we only wanted to maintain flat production for several years of that $6 billion. We don't anticipate that's what we will do but we do have the flexibility to do that.

Edward Westlake - *Credit Suisse - Analyst*

Okay, and then just coming back to the $60 Brent/WTI, I think in March you said at a slightly obviously higher price that you'd be doing $15.5 billion of cash flow in 2017. What's changed since then? Prices, opex, reductions, some disposals.

I'm wondering if anything else in your general sensitivity or price outlook has changed since March? To just bridge from that $15.5 billion down to the $10 billion I'm thinking specifically things like maybe LNG prices, other stuff that we should be thinking about when we model?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

I think we have lower prices all around besides just oil as well. We have lower natural gas prices assumed going forward also.

The biggest change, though, has come in just our estimate of the capital that it's going to be required to keep production flat going forward. And that's just the efficiencies that we've been able to achieve in the way the industry has evolved.

Edward Westlake - *Credit Suisse - Analyst*

And then just I'll sneak one last one in, a lot of focus on 2016 and 2017 efficiency gains, I mean obviously efficiency is great because it improves returns without any capital cost. There will be inflation but what do you think if the industry is going to be focused more on efficiency than it perhaps has been in the past, as you look beyond 2017 do you think you can still continue to drive efficiency through the business?

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

Well, without a doubt I mean these reductions they need to be sustainable both on the capital and on the operating cost side. The level of inflation that we see as we turn around here will clearly be a function of just how quickly the turnaround comes and how quickly we put equipment back to work.

But the underlying sustainable reductions and particularly in the operating cost here that we've talked about and when I talked about some of the organizational portfolio and optimization effects, those are going to be sustained. And we should be able to continue to show further efficiencies in those areas as we move into the time beyond 2017.

Edward Westlake - *Credit Suisse - Analyst*

Thank you.

Operator

Pavel Molchanov, Raymond James.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Guys, thanks for taking the question. I appreciate the detail.

On APLNG as with all LNG projects you're well aware there was a lot of concern about the sanctity of offtake agreements. And I'm wondering if we can get your updated thoughts on the shape of your offtake agreements, any adjustment provisions that we need to be aware of and generally how pricing is shaping up?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Well, yes, the agreement we have with Sinopec who's our main underlying buyer is a take-or-pay agreement. It's linked to oil prices, Brent, JCC prices like most of the contracts are.

THOMSON REUTERS

They've asked -- it's got a -- it's got a downward tolerance of about 10% that the buyer can elect to exercise. They've got diversion rights within China. They've asked for diversion rights outside of China which we've accommodated and said we would gladly help them on that but the contract is solid.

They've said they will adhere to the contract. We're not too worried about that.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Okay. Is there a look-back provision on the JCC pricing or is it in spot real-time?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Well, it lags a month in terms of pricing if that's what you're referring to. If you're referring to when is there sort of there is a six-year period of time after the contract gets started where the parties can sit down and talk about the contractual terms like a normal LNG contract.

Pavel Molchanov - *Raymond James & Associates - Analyst*

Okay, that's clear. I appreciate it.

Operator

Roger Read, Wells Fargo.

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

Yes, good morning. Sorry I had to get off the mute button there.

I echo the prior comments. Definitely a very helpful presentation.

As you're looking, I guess this question is for Jeff. The rating agencies I know you're in relatively regular discussions with them, can you give us an idea what the impacts would be if you were to drop down a level or two in the ratings in terms of what would be the financial impacts we'd have to think about?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

The way we think about the rating, when we talk about wanting to have an A credit rating it really describes a level of financial flexibility that we as a company feel like it's appropriate for us to have to be able to maintain some consistency in our capital investments and to be able to be comfortable that the dividend is very sustainable as well. So it's really a decision that we've taken to adopt that level of financial flexibility and the rating is just a reflection of that. There's not any real consequence if we would go from the single A flat that we are now to an A minus to a BBB plus.

We don't feel like that, debt cost us a little bit more. We still would have access to capital markets but we just don't have the same level of financial flexibility as a company which we talk about working in a volatile price environment and probably a volatile price environment going forward we feel like that's an important aspect for us to have.

So it's driven by that and not by really any additional costs that we have. We have strong liquidity, we have liquidity that has no -- we don't have financial covenants, we don't have any kind of adverse change clauses or anything like that in our liquidity as well.

So it's not really driven by economics or liquidity. It's driven by just a desire to have the financial flexibility to deal with a volatile world.

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

Okay great, thanks. And my unrelated follow-up, the asset sales we know what you're completing this year, it looks like targeting $1 billion to $2 billion both in 2016 and 2017 if I understood correctly. I was wondering if you could give us an idea out of the total resource chart, the 44 billion barrels equivalent, where are the asset sales that you're targeting really where they come out of on that pie chart?

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

The asset sales that we announced today represent about 170 million barrels that were reserves, so they come out of the reserves part of that pie chart. The asset sales that we've talked about for next year are the deepwater and Block B in Indonesia.

Block B I don't have the number off the top of my head frankly but that will come out of reserves, it's relatively small. And deepwater we don't have any reserves.

In that pie chart the total resource was about 500 million barrels that was in deepwater. So if we completely exit deepwater, so about 500 million barrels that was right at the very high end of the $75 a barrel range for cost of supply.

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

Great, thank you.

Operator

Ryan Todd, Deutsche Bank.

Ryan Todd - *Deutsche Bank - Analyst*

Great, thanks. Good morning everybody.

Maybe if I could follow up one more on the longer-term capital and production implications. With the implication and the ability to cut down close to $6 billion in 2017 if you're holding everything else relatively flat besides a couple of big moving pieces, in 2016 US production at the current levels I think you said is declining 3% annually.

As we look forward over the next few years if you were to keep the US at that level, is that a reasonable annual rate of decline? Do you see that shallowing out over the next few years? And what would be I guess in a longer-term $6 billion view would Alaska be a moderate offset of moderate declines in the Lower 48 or how do you view those?

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

The primary source if we were to hold capital is $6 billion, the primary source of offset to decline in the Lower 48 would actually be Canada coming from our oil sands business, at FCCL. By 2017 Surmont will be fully ramped up, APLNG will be fully ramped up, so the source of growth that would offset decline would for the most part be in FCCL in fact.

I can't remember, Ryan, what the first part of your question -- the declines, if we were to hold capital flat at $6 billion we'd see probably an increase in decline rate in the Lower 48 relative to the 3% that we're talking about in 2016.

Ryan Todd - *Deutsche Bank - Analyst*

Okay, thank you. That's helpful.

Then maybe it sounds out of place considering all the talk about cutting but from an acquisition of resource point of view, as we move here through the trough, how much interest is there on your part in smaller scale acquisitions in terms of beefing up certain parts of the resource base? Or is that effectively off the table for now?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

Well I think in this kind of a price market we're looking at it, we follow the acquisition, we follow all the companies pretty closely. But really anything we're doing we're in the market every day doing smaller bolt-on kinds of things to the market. If your question is some of the larger kinds of things we really don't have to do that.

As Matt's described in our captured resource base we've got a lot of opportunities and a lot of low cost of supply opportunities to organically grow the company. So anything that we have to do has to pass a pretty high hurdle and be substituted in the portfolio.

So we look at it, we watch it, we follow it but we don't have to go do anything. So we're happy exploiting the resource base that we have already captured in the company. Because it has lots of low-cost resource additions that can grow the company for a long period of time.

Ryan Todd - *Deutsche Bank - Analyst*

Great, thanks a lot. I will leave it there. It's been very helpful.

Operator

John Herrlin, Societe Generale.

John Herrlin - *Societe Generale - Analyst*

Yes, thank you. Most things have been asked. With your optimization of operations, is that all now in place, Matt?

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

Yes, I mean that's obviously an ongoing thing. The examples that we use there is that when oil price is $100 a barrel the optimum operating efficiency is equal to the maximum operating efficiency typically. But when oil prices are $50 a barrel or below then the optimal operating efficiency is a bit lower than that.

So it's calibrating our operating levers are calibrated to make sure that when so for example if a piece of equipment fails on a Sunday morning do you bring a crew out to fix it on a Sunday or do you wait until Monday to do it? Well, you don't need to in most cases you can wait until Monday to do it and you don't pay the overtime. So that's the sort of thing that I mean by optimizing for the price environment that we're in.

John Herrlin - *Societe Generale - Analyst*

Okay, thanks. Regarding the comments from the rating agencies, do they have a higher comfort level with conventional reservoirs because they have a lower decline rate and given the maturity of your asset base so there's greater certainty of output?

Jeff Sheets - *ConocoPhillips - EVP, Finance & CFO*

In our discussions with them I've never really heard them talk about preference for one type of production or the other. What they really value is size and diversification. That comes through in their commentary.

They are both pretty good and getting better at providing a framework about how they determine ratings. And you can see when you go look at their frameworks whether it's Moody's or S&P that there is a very large weight put to diversification and to size.

So I think it's more that than it is any particular type of production. I haven't heard them express that preference.

John Herrlin - *Societe Generale - Analyst*

Okay, thanks, Jeff.

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

I think we have one more question, Christine. Am I correct?

Operator

Doug Leggate, Bank of America.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Thanks, guys, for squeezing me back in. I wanted to get back in queue. I just wanted to get some clarification on the disposal program.

$1 billion to $2 billion a year but you haven't really given us a timeline and I'm guessing it's a little bit unrealistic to assume that it's indefinite. So what's the practical duration of those disposals and how do you think about I guess selecting those assets and what I'm thinking is 5% of production for 1% of cash flow appears to be the disposals announced today. So how do you characterize what qualifies as non-core? And I do have one final follow-up please.

Ryan Lance - *ConocoPhillips - Chairman & CEO*

We're a pretty large company, nearly 9 billion barrels of reserves. As we go through time and as we produce the assets out we're constantly trying to renew the portfolio. So we're adding capital to the front end.

We just think in a portfolio our size we've probably got $1 billion to $2 billion of assets every year that reach a point that they are not competitive for the capital in the portfolio at a mid-cycle price that we're basing the company on. And when we see that and we get approached by it we don't want to ride these assets down to the last drop of oil and then take on the abandonment liability.

There's other people that are willing to invest in those assets and carry them on forward in the business. So we just look at, I don't have a timeline to say when this would quit or could we go another three or four years. I just think in a company our size with the portfolio that we have we ought to expect and we've got a systematic process in our company to make sure that we're scrubbing the portfolio every year and going through it and making sure that we're getting full value.

We're not going to fire sale anything. There are some assets that we had on the market this year that we chose not to sell. We chose not to sell because we didn't get full value for what we thought we could go and spend the capital and invest and exploit the assets.

So we just have a rigorous process in the company every year to make sure that we're always culling the bottom end of the portfolio. And history would show us that that's $1 billion to $2 billion a year.

Doug Leggate - *BofA Merrill Lynch - Analyst*

Okay, but is that a process, have you already identified what you think those assets are, Ryan, or is it kind of an ongoing process?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

We know what the bottom end of the portfolio is. We know where it's at and we know what it's worth to us.

Doug Leggate - *BofA Merrill Lynch - Analyst*

So in that case can you put some kind of timeline on it then? So is it one year, is it five? Here's what's behind my question.

I guess is my follow-up I guess. Just as inappropriate asking about acquisitions might be right now, if you did let's say five years at the high end of that range, so almost 20% of the market cap of the company. I'm just trying to get a feel as to is that a kind of practical level? Because buybacks come into the frame then I guess as when use of those proceeds and I'm just trying to get a frame for ultimately what that magnitude that you've already identified could look like?

Ryan Lance - *ConocoPhillips - Chairman & CEO*

I'm not going to commit to a timeframe. We just have a pretty rigorous process that's going to look through it.

It could be nothing in a year and it could be $2 billion in a year. I think it's just reasonable to show a bit of a range there and we'll continue on for the next few years.

Doug Leggate - *BofA Merrill Lynch - Analyst*

All right, it was worth a try. Thanks.

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

Thanks, Doug. And I think that closes out our queue. I just wanted to thank everybody again for participating and wish all of you a very happy holidays.

By all means call investor relations if you have any other follow-up questions. And Christine, I will turn it over to you for closing comments. Thank you again everybody.

Operator

Thank you. Thank you Ladies and gentlemen, this concludes today's conference.

Thank you for participating. You may now disconnect.

Editor

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