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REP.MC - Q3 2018 Repsol SA Earnings Call

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## PRESENTATION

### Operator

Hello, and welcome to the Repsol Third Quarter 2018 Results Conference Call. Today's conference will be conducted by Mr. Josu Jon Imaz, CEO. A brief introduction will be given by Mr. Ramón Álvarez-Pedrosa, Head of Investor Relations. Please note that today's call will be recorded. I would now like to hand the call over to Mr. Ramón Álvarez-Pedrosa, Head of Investor Relations. Sir, you may begin.

### Ramón Álvarez-Pedrosa - Repsol, S.A. - Head of IR

Thank you, operator. Welcome to Repsol Third Quarter 2018 Results Conference Call. As the operator said, today's call will be hosted by Josu Jon Imaz, our Chief Executive Officer, with other members of the executive team joining us here in Madrid. Before we start, I advise you to read our disclaimer. During this presentation, we may make forward-looking statements, which are identified by the use of words such as will, expect or similar phrases. Please note that actual results may differ materially depending on a number of factors as indicated in the disclaimer. I will now hand the conference call over to Josu Jon.

### Josu Jon Imaz San Miguel - Repsol, S.A. - CEO & Executive Director

Thank you, Ramón, and thank you to everyone online for attending this conference call setting out our third quarter results. Today I like to cover the following principal topics: Firstly, I will start with the key messages and main operational for the quarter; secondly, a summary of the financial results; and finally, an update on outlook for the end of the year.

Let me begin with the key messages of the quarter. At the macro level, the market environment has remained broadly in line with the previous quarter. Brent price consolidated its recent recovery, averaging \$75 despite volatility during the period. Third quarter EBITDA at CCS and operating cash flow amounted to EUR 1.9 billion and EUR 1.6 billion, respectively, without a material working capital buildup this quarter. The cash generated by our operations more than cover our CapEx, interest payments, dividends and the purchase of EUR 0.4 billion of treasury shares under our buyback



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program. Net debt at the end of September stood at EUR 2.3 billion, a EUR 400 million reduction from the previous quarter. Moreover, the liquidity amounted to around EUR 9.3 billion, including cash, deposits and undrawn committed credit lines.

Let me underline that earlier this week, Fitch improved its outlook for Repsol from stable to positive, maintaining its BBB rating. Upstream operations continue to be focused on the successful development of our price, on time and on budget, benefiting from a better commodity scenario and progressing on the high grading of our portfolio. Planned maintenance and lower volumes in Venezuela had a negative impact on quarterly production. Under a strong oil price scenario, Downstream results were in line with the second quarter, impacted by the ongoing challenging environment in chemicals and, of course, the seasonal effect in the results of the LPG and Gas & Power businesses. In Low Carbon, we continue progressing towards our strategic objectives, and the transaction with Viesgo is expected to be completed early November. In addition, we have recently acquired the permits to develop a 264-megawatt solar project in Spain. With these 2 transactions, we will reach more than 70% of our 4.5 gigawatts of unregulated low-emissions generation capacity target to 2025.

In Corporate on September 4, we started implementation of our buyback program in connection to the share capital reduction approved by our Annual General Meeting in May. Including the shares purchased before the implementation of the program, again, of September, Repsol had bought 32 million shares of the total 68.8 million shares to be amortized. The share capital reduction will be executed within a month after the buyback program is completed. Finally, on September 20, as you know, CaixaBank announced its intention to divest its 9.3% stake in Repsol after 22 years as shareholder of the company. At the time of the announcement, half of that stake has already been sold in the market. The remaining position is being sold in an orderly way through a disposal program that will be complete before the end of first quarter of 2019.

Moving now into the operational highlights of the quarter, starting with the Upstream. Our accumulated crude realization prices to September have evolved in line with the recovery of the main crude benchmarks in 2018. In contrast, gas realization prices have improved by 16% compared to an 8% decline of the Henry Hub index. This is a consequence of our limited disposal to North American gas spot prices as most of our production is linked to Brent or another liquids and gas references.

Our portfolio actions in the quarter included the exit from our positions in U.S., Mid-Continent, Romania and Angola. Third quarter production was impacted by planned maintenance in several assets and lower volumes in Venezuela due to lower gas demand in the domestic market. Quarterly volumes averaged 691,000 barrels of oil equivalent per day, a 4% decrease quarter-on-quarter and in line with the same period of 2017.

In Libya, despite security conditions still being a concern, production averaged 35,000 net barrels per day. This is a 3,000 barrels per day reduction compared to the second quarter and 10,000 barrels higher than in the same period of 2017. Up to the end of September, the total group production has averaged 713,000 barrels per day. Development activity includes the ramp up of Reggane in Algeria, one of our most significant projects in Africa, which reached its plateau production level in August.

In exploration, a total of 5 wells were finished in the quarter, 2 of them are currently under evaluation, while the remaining 3 were deemed unsuccessful.

Moving now to the Downstream and starting with refining. The margin indicator averaged \$6.70. Compared to the second quarter, the indicator creator was impacted by, in other words, heavy-to-light crude differentials, partially offset by the strengthening of the main product spreads. Completion of all major planned maintenance in refineries in the first half of the year allow us to increase our utilization rates in both distillation and combustion units. In addition, with all conversion capacity on stream during the full quarter, our unit CCS margin was able to generate a premium to the indicator. The chemicals business continued to face a challenge in international environment, mostly driven by the increase in the price of naphtha and the production volumes were also affected by the turnaround of Sines that started at the end of July.

Compared to the second quarter, the result of marketing business was positively impacted by the driving season in Spain and Portugal, while seasonality affected LPG and Gas & Power negatively. Finally, our business in Peru finalized the development of the new gasoline desulfurization unit at the La Pampilla refinery, which started operation in October. This project completes a EUR 741 million investment that includes the diesel, desulfurization unit that started up in October 2016.



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Moving now to the financial results. I'll summarize the main figures for the third quarter of the year and how they compare with the same period of 2017. Third quarter 2018 CCS adjusted net income was EUR 588 million, EUR 60 million higher than in the same period in 2017. Upstream adjusted net income rose EUR 368 million, a EUR 220 million increase compared to the third quarter in 2017, driven by higher prices and lower amortization, partially compensated by higher exploration expenses and taxes. In the Downstream division, the CCS adjusted net income was EUR 336 million in the quarter, EUR 166 million lower than in the same period of 2017, mostly due to a lower contribution from chemicals and refining and lower results in LPG and Gas & Power. In Corporate and others, the adjusted net income was EUR 116 million negative, probably in line with the same period in 2017. For further detail on Repsol's results, I encourage you to refer to the financial statements and accompanying documents that were released today.

Before closing this first speech, let me now review the outlook to the end of 2018. Considering our progress during the first 9 months of the year, there are no material changes to our main financial and operating objective for 2018. Our previous EUR 4 billion guidance of total capital expenditure now sits at the higher end of our planning assumption range. I mean, capital discipline is a must, for me and for my management team, and we are going to deliver on that.

The efficiency and digitalization programs are progressing across the whole organization, having already delivered by the end September the full year targets set for 2018.

In Venezuela, during the month of October, we have already received two cargoes from PDVSA to cover outstanding payments in Petroquiriquire. Additional payments for Cardón, Petroquiriquire and Petrocarabobo are expected in November, allowing us to reach our cash objective for the year.

Looking at our projects, fourth quarter drilling activity in the first phase of Akacias in the CPO-9 block in Colombia continues with the objective of doubling production in 2019 with a potential FID for the full development of the field in first half of next year. In the Marcellus, drilling activity will be supported with addition of a second rig starting in the fourth quarter. In Baskin, in the Gulf of Mexico, the 2 wells of the first phase have been drilled and development, and we'll continue towards achieving first production in 2019 -- in the first half of 2019.

In Alaska, our two-well well appraisal campaign in the Pikka area is expected during the coming winters window in order to confirm recoverable volumes and test the development concept. The appraisal phase of Sagitario in Brazil is expected to start during the first half of 2019. Finally, after getting the final investment decision, the development of Angelin in Trinidad and Tobago is progressing on track with first gas expected during the first quarter of 2019.

In the Downstream unit, the Refining Margin Indicator has averaged around \$5 in October, following the sharp reduction in gasoline spreads and narrower heavy-to-light crude differentials that these effects have been partially reverted at the last week of the month, and the indicator is today at a level of \$6.40, \$6.50 per barrel, and that is the level in these last days of October, reverting this 2, 3 weeks where we suffer these effects from the market. In chemicals, we have adjusted our full year EBIT forecast from EUR 350 million to around EUR 290 million in 2018, driven by the worst environment and unexpected operational issues earlier in the year.

In conclusion, as we face the last quarter of 2018, we are confident on delivering on all the key objectives set in the first year of our strategic update. Supported by an improving commodity price scenario, Upstream has become the main cash flow contributor of the company. This division continues to work to further reduce its cost base and high-grade its portfolio, sustaining current production level and developing our projects in an efficient way. This better price environment is helping us for accelerating our portfolio rotation, completing the exit from positioning noncore assets or from areas where we don't have an optimal escape. At the group level, our accumulated result through September demonstrate the benefits of our integrated model. Coming from record levels of refining and chemical mergings in recent years, the Downstream division continues to generate significant cash flow in a much higher oil price scenario.

Moreover, Repsol is perfectly positioned to benefit from the upcoming IMO regulation. And we continue working towards optimizing refining operations to maximize the value captured by 2020.



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The chemical business enjoyed a very favorable environment in the past 3, 4 years, leading to a record level performance in 2016 and 2017. The significant positive results generated in 2018 under a more challenging scenario, not only from the international margins point of view, but also from the operational point of view, that was overcome and is over, are solid evidence of the turnaround achieved in this business by investing during the previous down cycle. In Low Carbon, we are quickly delivering on our targets, and the Viesgo transaction will be the core of our inorganic growth to 2020, becoming the cornerstone of our future low-emission Gas & Power business.

Let me finalize by underlining that under a sustained higher oil scenario, our strong balance sheet and financial flexibility will allow us to accelerate our projects, while delivering our objective of increasing shareholder compensation by 8% annually as committed in our recent strategic update.

With that, I now hand the call back to Ramón, who will lead us for the question-and-answer session. Thank you.

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Thank you, very much, Josu Jon. Before moving to the Q&A session, two previous advises. One is that, in case you're running to technical problems during the webcast or conference call, please address any problems to our e-mail address, [investorrelations@repsol.com](mailto:investorrelations@repsol.com), and we will contact you immediately to try to solve it. Also before moving to the Q&A session, I would like the operator to remind us of the process to ask a question. Please go ahead.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions)

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Thank you. Let me move to the Q&A session then. Our first question comes from Flora Trindade from CaixaBank BPI.

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**Flora Mercia Trindade** - Banco Português de Investimento, S.A., Research Division - Analyst

I have a couple of questions on guidance. You have maintained the CapEx target of EUR 4 billion. But considering the CapEx in the 9 months, it should mean a strong concentration in Q4. Is there a specific reason for this concentration? Or are we likely to see a lower figure by year-end? And then the second question is on the EBITDA. I think you had previously mentioned EUR 7.9 billion target for the EBITDA. Can you just update that with the recent cut in chemicals and also the update on oil prices we are seeing?

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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Thank you, Flora. I mean, first of all, let me say that CapEx is going to be EUR 4 billion, as I said before, that is the higher range of our approach today, at December 31. And in this CapEx is, of course, included a EUR 750 million that we are going to pay for Viesgo, the asset of Viesgo in coming days. So I mean, the main reason of this concentration, of course, is this additional CapEx. And as I said before, I mean, EUR 4 billion is the higher range of our expectation of our guidance today because, as I underlined before, I mean, capital discipline has to be a must in the company. That is written on a stone in the management team and the whole people from this company. As we said before in the strategic update in June, we are going to be very conscious in the disposal, the application of CapEx, guaranteeing that the return is going to come. And let me say that one of the main reasons for this reduction in the CapEx figure is that we are more efficient than expected delivering the growth projects coming mainly from the Upstream side, but also projects coming from the Downstream. I mean, we are going to gain EUR 300 million in efficiencies over the whole year, guaranteeing that the products are on track. We are guaranteeing that the production projects in the Upstream are on track with no delay.



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The CPO-9, the first phase is going to -- is growing and is going to be finished in the first quarter of 2019 to take the FID in the first half of 2019 of the second phase. The Baskin are going to be on track. The IME project is going to be also on track. We are going to apply the second rig of the Marcellus in the last quarter. I mean, all the growth is on track. We are very efficient applying this CapEx and that is going to be our -- the higher range of the figure at the end of the year. As you said, I talk about EUR 79 point billion (sic) [EUR 7.9 billion] for the EBITDA of the year in July. I mean, today that is also the guidance for the end of the year, EUR 7.9 billion of EBITDA at the end of the year. We maintain this guidance, it's true. As you said that in the chemical side, I remember that I talked about exactly EUR 350 million of EBIT, and we are going to be in, all over figure, EUR 290 million, more or less, EUR 60 million below the figure that we commit as guidance in July. The main reason is going to be that the turnaround of Sines was a bit longer than expected and also the international margins level we have experienced over the last weeks. But let me say that after overcoming this reliability problems and operational and maintenance and turnarounds periods we have in our crackers. I mean, even at these oil prices, I think that talking about EUR 350 million of EBIT of our Chemical business for 2019, it could be a good approach. Thank you.

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Thomas Klein from Royal Bank of Canada.

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**Thomas K. Klein** - RBC Capital Markets, LLC, Research Division - Senior Associate

I just had one on Venezuela. You were talking about it before and you also mentioned you had a negative impact on production in the quarter. But can you quantify that a bit more, and provide an any more color?

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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Yes, Thomas, of course. In Venezuela, I think that you know that the economic and social situation is complex here. And over this quarter, we were impacted by a reduction of production not because we had any kind of -- any decline in the gas production, not because any operational problem, but because some of our clients that are using this gas for producing power in thermal plants and they were shutdown. So we have a reduction of demand because of the operational problems in some plants that are buying our gas in Venezuela. For that reason, the gas production was at around 20,000 barrels equivalent per day in the first quarter. And let me say that -- I mean, on top of that, I said before, we have some turnarounds and maintenance problem in -- and planned maintenance periods in the U.K. in MonArb. We also have something like that in Marcellus, in the PM3 in Malaysia, in BPTT in Trinidad and Tobago and so on and also in Norway in Gudrum. But this factor of the reduction of production in Venezuela due to this reduction of demand was behind a main part of the production reduction in the third quarter. But as I said, I mean, even in this complex economic context in the region and in the country, I mean, we have some positive signs coming from Venezuela in October. We were paid with 2 cargoes that we have already received them in our plants. And on top of that, they have committed 2 more cargoes in the framework of financial agreement of Petroquirique in coming weeks before the end of the year and 2 more related to the receivables of the gas of Cardón. I mean, I don't know what is going to happen, but taking into account, let me say, a prudent approach to the picture, I think that the target of being neutral in free cash flow terms in Venezuela this year is going to be there.

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Thomas Adolff from Crédit Suisse.

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**Thomas Yoichi Adolff** - Crédit Suisse AG, Research Division - Head of European Oil & Gas Equity Research and Director

Couple of questions from me, please. Firstly, just on net debt. Obviously, you had very strong cash flow from operations this quarter. We just saw net debt go down to EUR 2.3 billion. Remember, your guidance previously for year-end net debt was around EUR 3.5 billion, and I can get to that if you do quite a bit of buybacks in the fourth quarter. Can you perhaps talk about what -- where you see net debt ending, and maybe discuss the moving parts, please? And secondly, just in Downstream, yes, refining margins seem to have recovered last week and including this week, but I



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wonder, since you use about 50% of heavy crude with Maya being possibly the best indicator for your indicator margin, whether it's reached a level where it makes sense to go to alternatives?

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Thank you, Thomas. I mean, first of all, I think that the figure that I have in mind that I talk about, but is very close to the figure you said, it was EUR 3.6 billion in July, but anyway EUR 3.5 billion, EUR 3.6 billion, you know that a cargo delivered in the last day of December could move to EUR 100 million, EUR 150 million up or down the net debt figure. I mean, we have to take into account that this fourth quarter, we are going to cash out our EUR 750 -- EUR 750 million, sorry, to pay the assets of Viesgo. On top of that, we are going to complete and coming before December 21, and taking into account the rhythm we have that on October 26, we already have two, nine more -- sorry -- 8 or 9 million of additional shares to be bought. So that is -- that means that we are going to need EUR 600 million in the quarter for the buyback. And on top of that because the divestment of Gas Natural, we have to anticipate this quarter, in the fourth quarter, EUR 400 million to the Spanish treasury, and we are going to be paid back in January 2020. So we had anticipation of taxes. So taking into account this combined effect of EUR 800 million approach to pay Viesgo, EUR 750 million, EUR 400 million for the anticipation of taxes for the divestment or disposal of Gas Natural plus EUR 600 million for the buyback in this quarter. Taking into account these figures and taking into account what we forecast in terms of cash generation coming from the operations in this quarter, I think that this figure of EUR 3.6 billion, I mentioned before, could be our most accurate approach for the end of the year, but, as I said before, taking into account that we're going to anticipate EUR 400 million that is going to come back and guaranteeing the whole fulfillment of the buyback program. So EUR 3.6 billion, the figure, I anticipated in July, is today my best approach. But as I said before, we are fully focused on the cash generation and on the efficiency in CapEx. So myself and the whole team is going to do our best, if we could, of course, to improve this figure. Talking about the refining margins, I mean, today we are at \$6.5 per barrel in the current business scenario. The average in the last -- in the first 9 months of the year has been \$6.9 per barrel. I mean, I think at the end of the year, we are going to be very close to this figure. Perhaps, we could be \$0.1 or \$0.2 below because the first 2, 3 weeks of October, that as you know, we were -- I mean, in October, we could have an average of \$0.5. So that could impact it perhaps in \$0.01 per barrel or something like that in the average of the year that we're going to be there. I mean, you are right. This spread of heavy oil is impacted either in a positive or negative way in our feedstock. We have seen over the last 3 years, I mean, ups and downs. We are adapting our programming everyday, depending on the spreads and the prices in the market. I mean, we see the increase in the feedstock of medium API crude oils, Urals and so on, and reducing the heavy oil, we are optimizing the basket. I mean, we are going to do that, be sure about that. By all in all, I think that today, the refining margin is not going to be far from 8 -- \$6.8 -- sorry, \$6.9, \$6.8 per barrel at the end of the year. And we can't forget that we are impacted by the feedstock in terms of heavy oil, but also 55% of our deal is middle distillate. I mean, this winter that is now coming and that they arrive to the Iberian Peninsula last week, very hard terms, is going to have an impact on the middle distillate spread. So, all in all, we are going to be there.

**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Lydia Rainforth from Barclays.

**Lydia Rose Emma Rainforth** - Barclays Bank PLC, Research Division - Director & Equity Analyst

Two questions, please. Firstly, in this [trusty] presentation, you did talk about the extra cash that you use to accelerate the growth projects that you have. Can I just ask when are you prepared to trigger that acceleration? Or what would make you to go actually through (inaudible) more projects? And then secondly, and of course, a slightly boring question, but what was behind the strong equity affiliates contribution in the quarter?

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Lydia, can you repeat the second question? The second one, please, Lydia. I had some problems due to sound.



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**Lydia Rose Emma Rainforth** - Barclays Bank PLC, Research Division - Director & Equity Analyst

I am sorry. The equity affiliates contribution looks very strong for the quarter. And I don't know if that was just the U.K. and the Sinopec -- or the Sinopec JV doing particularly well.

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

So going to your first question, I mean, first of all, Lydia, let me underline that I have here in front of me, I mean, in my office here and everywhere that cash flow increase that we committed in our strategic update coming from operations. And I mean, this target of improving EUR 1.9 billion by 2020 per year, the cash flow coming from the operations at a flat price of commodities. I mean, we take the case of \$50 per barrel is going to be written on a stone in every corner of the company in coming 3 years. And let me say, in the first half of the year, and I anticipate that this effect that the \$20 per barrel more in Brent price terms coming from the Upstream, they were going to be used to build the inventories of the Downstream because the weight that Downstream has in Repsol. I mean, we are going to start seeing this cash effect in the first quarter, and we're there. We're on track. And we are going to fulfill what we committed in our strategic update. We are going to see quarter-after-quarter better environment sometimes, worse environment sometimes, but we are going to do our best to deliver what we committed in cash terms in our strategic update. That is the main target, that is the main driver and that is the real objective I have. And as you said, Lydia, if we fulfill and we deliver what we said, we are going to have additional cash because, of course, we are going to fulfill and we are going to deliver the buyback program for the whole 3 years period to avoid any kind of dilution coming from the scrip dividend, but on top of that, we are going to use this cash for accelerating some projects. Some of them, of course, the commercialization site in the Gas & Power in Spain, now that we are integrating the asset of Viesgo, the service station program in Mexico, the trading expansion program, the international lubricant expansion program and, of course, we have also some growth projects in the Upstream, potential bolt-on projects in areas where we could have synergies, like U.K. and so on, the potential acceleration, I mean, in the Marcellus, where we are going to invest in the second rig this quarter, that is going to add. I can't say the exact figure, but 12,000, 14,000 barrels per day in gas production in the Marcellus. We are going to analyze what we could do in the future development in the Gulf of Mexico and thinking in the Buckskin, in León, in Shenzi and so on. And of course, it will be our target to analyze the possibility to take a potential FID in Sureste Illizi in Algeria also in 2019. On top of that, we are going to accelerate the development of the CPO-9 in Colombia after the early development we are promoting in this last month. So we have projects for that. The organic growth to fulfill growth we commit in our strategic update is going to be the priority. And let me say, we have the financial flexibility to do that. And the only thing we are going to look for, of course, is the high return of these projects to invest in. And talking about the affiliate companies, I think -- and we could check this figure later in light with the IR, but we are talking mainly from Trinidad and Tobago, BPTT, Brazil, I think that Brazil, the JV we have with Sinopec is impacting in a very positive way, and we also have the JV in U.K. As you could imagine, Lydia, at these oil prices, U.K. and Brazil are 2 JVs that are increasing in a quite significant way the profits in this quarter. Thank you, Lydia.

**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from (inaudible) from Bank of America.

**Unidentified Analyst**

I had 3, please. First one on working capital. I guess, for the first 9 months of the year, you've had quite a significant build and with limited change over the third quarter. And I think at the second quarter results, you mentioned you expected about EUR 0.5 billion of that working capital to unwind over the course of the year. Is that still a valid assumption going forward? Secondly, on Venezuela, can you just remind us on where the receivables stand at the end of 3Q? And whether the cargoes that you received in October had much of an impact on that number? And then finally, just looking at the trading business in the fourth quarter, how would you characterize your expectations on performance there because we've seen trading deteriorate over the course since the beginning of the year? So I wondered if you had any comments on that?





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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Thank you, (inaudible). I mean, first of all, the working capital has been flat in the third quarter. I mean, as I said before, we increased in EUR 1.4 billion the working capital over the first half. And I mean, all in all, we could think that more or less EUR 800 million could be associated to inventories due to the increase in commodity prices; EUR 200 million could be linked to the growth in some commercial businesses of the Downstream, including the working capital there because of the inventory effect; EUR 300 million over the whole year could be associated to Venezuela and receivables from that country; and EUR 100 million could be linked to the price effect on inventories in the (inaudible) site. So EUR 1.4 billion over the first half of the year and flat in the third quarter. I mean, in terms of working capital, I work on the assumption that we are going to be also flat at these oil prices in the fourth quarter. We are going to work on those assumptions. I mean, but you need -- you know, I mean, one cargo, the last day of the year could move this picture in EUR 100 million, EUR 120 million or EUR 80 million. That is our target for the end of the year. For now on, I mean, we are not building working capital, we are not building inventories. Talking about the trading business, I mean, the trading business for Repsol is performing in a good way. It's increasing the -- in terms of P&L. Perhaps there is an impact in seasonal terms because I have to check it, but the Gas & Power, the Gas American business in North America is included sometimes because of the trading activity, and you know that for that season for North America, our gas commercialization and our Canada port activity, I mean, is not in the best season in summer. But the trading is going to increase over these 3 years and is going to increase the contribution to the P&L of the company. And this year is going to be there. Sometimes that this is a volatile business, but the trend is clear for us. Talking about the receivables, I mean, as I said before, we could have today, at the end of the third quarter, a total exposure to Venezuela of \$920 million, EUR 800 million. So we are maintaining the total exposure we had before in the second quarter. Here we are including everything; equity, loans, receivables and so on. It's the total exposure in financial terms we have to the country. I think the receivables that -- in the third -- the receivables were -- the bills were paid in October. So they are not in the third quarter. I mean, no dollar coming from Venezuela in the third quarter. These cargoes arrived and came in October. And our expectation in November and December is being very prudent because I know what's the situation in economic terms is in the country, quite complex. And knowing that, I mean, I work under the assumption of maintaining this exposure to Venezuela at the end of the year in financial terms and being neutral in free cash flow terms over the whole year in Venezuela. That's the closest assumption I could give you now, I mean, taking into account that there are some factors that today, as I said before, they are not in my hands.

**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Alessandro Pozzi of Mediobanca.

**Alessandro Pozzi** - Mediobanca - Banca di credito finanziario S.p.A., Research Division - Research Analyst

I have 2. The first one is Libya. I think production in the country now is right above 1 million barrel. And I was wondering if we could say that the in Libya now looks more stable? And if it is, just wondering whether you'd be willing to deploy a bit more funds to grow volumes there? And I was wondering how much you're planning to produce from Libya during Q4? And also second question on the average gas realizations, as you mentioned, they performed really well. I was wondering if you can give us a bit more color on the various moving parts there? And also given that the Henry Hub now is around 3.2, 3.3, they should provide a nice boost to margins in North America, Upstream margins in North America. I was wondering perhaps if you can give us maybe an update on the economics in the Marcellus as well?

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Thank you, Alessandro. I mean, as you said, goods coming from the production in Libya is a good news. This quarter we have had an average of 35,000 net barrels per day for Repsol, 2,000 barrels per day lower than the average of the first 6 months because we had, in the last days of July, some security concerns in the area and we reduced the production. Our best guidance for the year, taking into account that we are talking about the country with a complex security concern, could be at around 38,000 barrels per day for the whole year. That means that the fourth quarter -- I mean, the asset is performing in the right way. I mean, the concerns about the stability of the country are there. But let me say, I think that this is important, the oil production in Libya, because Libya is taking the taxes and the cash coming from the operation and all that is helping to establish the country, improving the standard of lives of people. And I think that we are and we could enter in a virtuous circle in some way. But, as I said before, I mean, that is not in our hands. We see that the situation being complex, being challenging could be, in stability terms, a bit better than it



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was 2, 3 years ago. But anyway, I mean, we try, of course, to preserve the security of our people, the safety of our operations. And in this framework, we try to optimize the performance of the asset. And we are, of course, open to work in Libya, and we are also open, of course, in the framework of a reasonable risk return ratio to explore also new opportunities in Libya being present from the financial point of view. But I think that in the complex situation of the country, we have to work together and we are working together with the National Oil Company and with Mr. Sanalla to collaborate with them in order to improve the situation of the sector in Libya and increasing, of course, the standard of life of people in Libya because all that is also good news for the stability of the country. Talking about the gas prices, I mean, first of all, let me say that, if we take one the whole gas production of Repsol that you know is 66%, 67% of our whole production, 30% of this production is related to Henry Hub, 30% to some others, international hubs at BP, K-M and so on, 20% more or less is Brent, Brent-related directly and 20% local or fixed prices. I mean, talking, for instance, Spanish Henry Hub or Henry Hub -- sorry, Spanish -- I was thinking in -- the Spanish electric pull price or some other local contracts. So for that reason, you could see that even in other scenario word, the Henry Hub was down 8% this quarter. We increased in a significant way the realization price of our gas production. In the case of Marcellus, I mean, I have to remind that the breakeven of this second rig project is in \$2.4, \$2.5 per million of BTUs. That means that, taking into account, the current sum of \$3.2, \$3.3 per million of BTUs of the Henry Hub and the expectation we have for coming 2, 3 years, I mean, we are a quite -- we rely on the profitability of this second rig investment that is going to give us even at \$2.5, a positive free cash flow.

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Rob Pulleyn from Morgan Stanley.

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**Robert John Pulleyn** - Morgan Stanley, Research Division - Analyst

Just one question remaining from me, and apologies if it's being touched on throughout the Q&A. But if I remember, you have a strategy of actively emerging the Upstream portfolio and actually high-grading by years. I think the idea was to sell sort of 300 barrels, which are maybe less attractive to some buying 100 barrels, which were more attractive. Can you just give us an update on that strategy, whether that's still the case? Obviously, you've talked about CapEx plans and we see the progress there, but how about the active management of the portfolio?

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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

We have taken advantage of this quarter to, let me say, I am going to use perhaps an appropriate work to clean a bit our portfolio and to exit from some countries and some assets, where we had either low margins or low expectations. We exit from Romania in the third quarter. We disposed our Mid-Continent asset that it wasn't in the best quartile, let me say, of our portfolio. We disposed what we had in Angola, and we also disposed and we are in the process of permits and so on to conclude this process in coming months. Our assets in -- some of our assets in Southeast Asia mainly in the area of Papua. So that means that we are taking advantage of this situation to reduce the scope of countries where we operate to increase the margin per barrel. And as you said, we have to complement all that with perhaps a growth, a new acquisition. At the moment this growth is organic, the second rig of Marcellus, that was example. I mean, that I don't discard. I mean, some kind of prudent acquisition of new barrels, but let me say, I am only going to buy new barrels for the Upstream, if we could guarantee that even at low oil prices we could have good returns. And that means that if we are buying assets when the oil prices are \$70, \$75 per barrel, we have 2 options; I mean, to take the risk or destroy value for the future, and that is not going to be our option. I prefer, let me say, to be conservative, to be moderate, to be very prudent in the capital discipline -- in the capital allocation discipline; or we could add some investment and that is the way we are exploring of having bolt-on acquisitions, adding some new barrels perhaps in areas where we could have clear synergies, clear operational logistic synergies, or why not pull -- significant pull of tax credits from the past, where we could have, let me say, additional advantages related to some other potential buyers. I think we are exploring these possibilities, that is open, but I am going to be very prudent. My target written on the stone is to fulfill the strategic update, to rely mainly on the organic side to increase the cash flow coming from the operations, being very focused on digital, efficiency, capital discipline, maintaining the financial prudence in the company, and relying on the organic growth, but all that is compatible if we could have this kind of, let me say, opportunistic and bolt-on operation, where we could add new barrels with significant advantages.



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**Ramón Álvarez-Pedrosa** - *Repsol, S.A. - Head of IR*

Our next question comes from Matt Lofting from JPMorgan.

**Matthew Peter Charles Lofting** - *JP Morgan Chase & Co, Research Division - VP*

2, if I could. I mean, first, 5, 6 months on from the strategic plans, I mean, it sounds like underlying progress on the efficiency and digitalization-led cash flow initiatives has been very strong. If you look forward, what are some of the key next steps? How much cash flow do you now expect these programs to contribute in 2019? And is there a case where the more work you do on them, incremental upside starts to emerge? And then secondly, on chemicals, coming back to the outage at Sines and looking forward in terms of the operational outlook, can you confirm that Sines is now fully back and stable in term -- in utilization terms? And also outline the maintenance requirement in the chemicals business for 2019?

**Josu Jon Imaz San Miguel** - *Repsol, S.A. - CEO & Executive Director*

So thank you, Matt. I mean, in terms of efficiency and digitalization, my message is, we are on track we committed in June. Anyway, be sure that in February in the year presentation of results, I am going to take advantage to describe the figure in a more accurate way, showing that we are fulfilling the commitments we take in June. But I could anticipate that we had a target in the digital site for this year of EUR 90 million of new cash coming either from new margins or forecast production coming from the digital program. I mean, in this third quarter, 85%, 90% of this target has been achieved. And today, this EUR 300 million of new free cash flow coming from the digital, I anticipated, I committed, in June, by 2020. I mean, we are going to be fully on track. So if we take -- there is, let me say, on the slide, that I laugh a lot, that is in our strategic update in June we presented the increase of the cash flow coming from the operations over these 3 years, 2018, '19 and '20 -- by 2020, taking the assumption of flat commodity prices. I mean, my message is, we are on track of achieving the targets by 2020 we committed in June. Anyway, I am going to give you some more flavor and more accurate and precise figures about all that at the end of the year in the presentation of results. I am going to take advantage of this presentation to show that when we are talking about the efficiencies and digital. And I suppose that after some years of fulfilling all our commitments in term of efficiency, we have the reliability to say that, that when we talk about that, that is not blah, blah, blah. That is the whole effort of the company that is going to deliver these figures at the end of the year. Talking about Sines, yes, it was an operational penalty we had this spring, all that is sober. We are working in a stable way since July 25, 26, more or less. I mean, today, I was checking out in my iPad the figure in operational terms. Today Sines is operating at 95% of the operation. And, of course, this figure is going to be there. And the maintenance for 2019, I mean, thinking about the maintenance, we have some maintenance in the refining side in 2019, but mainly to prepare the plants for capturing, let me say, the wind force coming from the IMO in 2020. I remember that we have the FCC on the vacuum unit in Coruña in 2019. We also have the FCC of Petronor, all the hydro treatment, including hydrocracker of Cartagena in 2019. And it seems to me that we also have in the third quarter the maintenance period of Tarragona, the cracker of Tarragona in the chemical side in 2019. And I mean, I have some people from my team, I think, that I am not forgetting any relevant maintenance program in 2019.

**Ramón Álvarez-Pedrosa** - *Repsol, S.A. - Head of IR*

Next question comes from Michele Della Vigna from Goldman Sachs.

**Michele Della Vigna** - *Goldman Sachs Group Inc., Research Division - Co-Head of European Equity Research & MD*

2, if I may, The first question is on the Viesgo. You're going to close that transaction next month. I was wondering if you could give us some visibility of what you expect that to contribute to earnings in 2019? And how much you intend to invest organically in growing that business? And then secondly, a very clear message on increased activity in the Marcellus as you have lowered costs there. I was wondering if you could also provide us an update of activity in Duvernay? And whether you expect to increase to take on more rigs there as well?



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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Thank you, Michele. I am sure that you are going to understand my point. You know that I love to give all kind of details, how often have you seen that. Today, these assets are not legally from ours, are not from Repsol. It is difficult for me to say and to consolidate figures that are not in the hands of Repsol. I expect that we are going to -- in coming days, I'm not talking about weeks, in coming days, we expect to close the operational integration of these assets in the business of the company of Repsol and to launch the project of Repsol Electricity and Gas that is going to be the umbrella for managing these assets. I mean, I could say you, Michele, that we are not going to see big surprises because -- I mean, if you take the evolution of the electric pull price in Spain over the last 9 months has been over our assumptions and expectations. You also know that the assets we are buying of Viesgo, they are quite much between commercialization and generation. That means that -- I mean, having surprises is not going to be easy. And let me say that I am not going to say more because they are not our assets today. But no big surprises. And let me say the CapEx are going to be always moderate, as I said before, and always in the framework we committed in the strategic update in June. I mean talking about the Duvernay, I think that by the end of 2019 we are going to be close to take the FID -- I mean, we are focusing on the areas where either the condensate or the oil content is higher in the asset because you know that the gas price in Canada is not experiencing the best time. So the good news from Duvernay is that more or less 35% is oil production, 35% could be condensate and 30%, 35% could be gas. So we are going to focus on the areas with more liquids content and it seems to that by the end of 2019, we are going to be close to take the FID in the area of Ferrier East. And our second target that is Gilby perhaps could be at around 2021 or something like that. But I mean, I am, let me say, more sure about the Ferrier East part. We are analyzing and trying to (inaudible) area and that is going to come perhaps the new step in the progress in the development of Duvernay, Thank you, Michele. Sorry, excuse me, the Marcellus, I forgot it. I have here the note and I forgot, Michele. I mean, we are going toward now the second rig in Marcellus. I think that is okay. We have a quite ambitious gas program by 2019. I mean, we are going to increase our production in the Marcellus. I think that this year we could be producing -- and perhaps I asked my team to correct my figure if I am wrong, but producing 450 million cubic feet per day. Our expectation is to increase that 20%, this figure, in 2019 due mainly to the addition of this second rig in the Marcellus. Of course, we are always open. Be sure that in case of having a Henry Hub over the expectation we have, we'll try to use all this additional potential cash that are going to come from the commodity side to accelerate in an organic way these kind of projects. But I think today taking into account the assumptions for 2019 in commodity prices and so on, staying with 2 rigs in Marcellus is a prudent approach for us.

**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Next question comes from Irene Himona from Society Generale.

**Irene Himona** - Societe Generale Cross Asset Research - Equity Analyst

I have 3 quick questions, please. Firstly, Libya. Can you please tell us what the contribution was in the third quarter and in the 9 months to Upstream EBIT and net income? And secondly, LPG. I think it's your lowest quarter in about 8 or 9 years. I wonder if you can just remind us of how the price formula works in terms of the time lag before you are allowed to increase pricing? And what can we, therefore, expect over the next few quarters? And then finally, in marketing, the 9 months EBIT is a nice step up year-on-year. You do highlight that you now have 100 Mexican service stations. Are they making a material contribution as of yet? Or it's not relevant to the picture?

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Starting by Libya, please check the figure with the IR team, but I think that we are talking about a net income of EUR 95 million, EUR 100 million, more or less. But please check later the figure with -- because it's figure I have in mind, but you could check the figure. I mean, people are saying that we are there more or less, perhaps I was mistaken in EUR 5 million, but not more. The LPG, I mean, it's quite logical. I think that it's a conjunction of 3 factors. The first factor is the system. I mean, we are talking about summer. The second factor is -- sorry, mainly 2 factors, sorry. The first one is season and the second one is that do note that the LPG business in the Spain is regulated. We have a gap of 2 months between the real price of the LPG and the price we are translating or moving to the market, and when the oil price is going up there is a gap and we recover, let me say, this deficit of tariff, I am using not the right term in regulated terms, but we are -- this gap or this area, this surface, we are losing in the curve when we don't recover the price from the formula, this prices recover in coming months. That means -- that is the reason for the negative impact of the LPG business; first of all, season; and secondly, this gap coming from the application of a gap in the times some kind of [décalage] when the price is



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going up, all that is going to be recovered in coming months. So no concerns because, if we analyze our LPG business, we are maintaining our volumes, our market share and our revenues quite stable over the last years. Going to the second question, I mean, it's Mexico, this weekend, I mean, I remember I was talking to María Zingoni this weekend and she told me that we were achieving the 100 service station figure -- 120, sorry, this weekend. So we have 120 today. I think that we could have more or less 175, 180 at the end of this year. In 2018, there is no P&L positive contribution, but today our main assumption on guidance is that we are going to have a positive in 2019 according to the business plan we checked last week for Mexico. So positive P&L in 2019.

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**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Our next question comes from Yuriy Kukhtanych from Deutsche Bank.

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**Yuriy Kukhtanych** - Deutsche Bank AG, Research Division - Research Associate

2 questions from me, please. Following on, on affiliates question. Could you please describe us how cash in Repsol Brazil is distributed? And has it been launched to the parents, to Repsol and Sinopec, or is it going to be returned to parents via dividend? That would be the first question. And the second is, what is the targeted return on your solar investment? And how exactly are you going to develop that business?

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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

I mean, I am not able to give you an exact flavor, of course, you could check this figure with IR, but I think that there are two mechanisms. And one often is the distribution of dividends that is decided by shareholders. And second one, I mean, is the financial mechanism that is called euros, that is the interest on equity that is paid to the shareholders. I can't remember now the exact balance between both factors, but, of course, Yuriy, you could check all that with the IR team. Returns on solar investment, so at the moment we don't have any kind of investment, let me say. We acquired EUR 20 million of the -- we pay EUR 20 million to buy the pipeline to build this potentially 264 megawatts of solar project. And we are going to be -- as I said, when we presented the strategic plan, the returns are going to be at around 9% in terms of return of the project. And combining the project with the commercialization site, we are going to pay -- we are going to do much with the generation we are going to have. We are talking about returns that are going to be above 11%, 12%.

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**Unidentified Company Representative**

Our next question comes from Peter Low of Redburn.

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**Peter Low** - Redburn (Europe) Limited, Research Division - Research Analyst

Just one quick one from me.

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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

Sorry.

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**Peter Low** - Redburn (Europe) Limited, Research Division - Research Analyst

You've talked about potentially accelerating certain Upstream projects. Is that likely to have any impact on your existing production guidance of 750,000 barrels a day by 2020?



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**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

No, because, Peter, in case of accelerating some projects, we will take advantage to accelerate the high grading of the portfolio. I mean, this portion, let me say, the lowest quartile of our assets to improve and to take advantage of the sound -- to improve the quality of our portfolio. So managing our portfolio, and we maintain the guidance of production we committed in the strategic plan, perhaps improving, that will be our target, improving margins, improving the quality of portfolio, but maintaining the guidance of production.

**Ramón Álvarez-Pedrosa** - Repsol, S.A. - Head of IR

Thank you, Peter. Well, that was our last question. And at this point, I'd like to bring our third quarter conference call to a close. Thank you very much for your attention. And we will welcome you next year.

**Josu Jon Imaz San Miguel** - Repsol, S.A. - CEO & Executive Director

So thank you.

**Operator**

Ladies and gentlemen, this concludes the Repsol's Third Quarter 2018 Results Conference Call. Thank you for your participation. You may now disconnect.

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