OMV Q1 2021 Conference Call – Q&A Transcript

April 29, 2021

OMV published its results for January–March and Q1 2021 on April 29, 2021. The investor and analyst conference call was broadcast as a live audio– webcast at 11:30 am CEST. Below is the transcript of the question and answer session, by topic, edited for clarity.

OMV Group

CEO contract extension

Question by **Josh Stone – Barclays**:
Rainer, there was some news that you're not going to extend your term beyond 2022 for 1 more year. I was wondering if you have to say why not as there were some headlines that you were looking to look for 5 more years.

Answer by **Rainer Seele**:
Why not additional five years, I don't get it approved from my wife. That's a clear answer, yes? It's a tough application. And my family has asked me to spend more time with the family. You must understand, I am now more than 15 years CEO of different companies, and I was always living in airplane. Now I also would like to spend some time with my family in the garden, enjoying a good glass of red wine.

Question by **Thomas Adolff – Credit Suisse**:
I do apologize. I missed the chunk of your presentation. So I do apologize if I do ask a question that's already been answered. Rainer, you chose not to extend your contract next year. I won't ask what's next for you, but can we expect to get an update on the successor by, say, the end of the year?

Answer by **Rainer Seele**:
Thomas, you have missed my first answer because Matt was also asking me a question. I have to discuss with my wife, and these are always tough negotiations. You will get an update early next year, I would say.

Cash flow

Question by **Thomas Adolff – Credit Suisse**:
I think on cash flow, I think you've said, over time, you want to be generating more than EUR 5 billion in cash flow from operations. Presumably, this is a pre working capital figure. Considering you've done 1.7 in the first quarter and assuming kind of the chemical margins that we're seeing in Q2 can be sustained for a little bit longer than Q2, where should we expect cash flow roughly to finish the year?

Answer by **Rainer Seele**:
Your second question, absolutely right analysis. This is going to be a very cash-rich year for OMV looking down the road. Reinhard will give you a little bit more insight.

Answer by **Reinhard Florey**:
Thomas, just to clarify, our midterm target of more than EUR 5 billion in operating cash flow is a pre working capital number. Why is that? Because if we are planning to the future, we do not plan for the fluctuations of the net working capital. So that is more or less an assumption of a flat delta net working capital that we have in there. And you're right, if we are taking it pre net working capital this year, the 1.7 is a fabulous number, and it will not go away. However, we cannot expect that we have the same impact in the following quarter because, of course, also the effect that we see in the net profit from the effects of higher prices that have been rising in the first quarter have had an impact. This is the CCS effect which we are not expecting to replicate in the coming quarters. But even if you take the post working capital number of almost EUR 1.1 billion in this first quarter, this is an excellent number. And there, we are quite confident that we are keeping this level if economic environment keeps on pushing positively.

Deleveraging

Question by **Josh Stone – Barclays**:
If you just update us, there was on disposals, talk about a third package to be announced this year. Is that still the case?

Answer by **Reinhard Florey**:
First of all, of course, we are concentrating on the first and the second wave of our disposals. For the first wave, and those are the 3 divestments that Rainer has spoken about that have been signed already in 2020 and will now close in 2021, bringing proceeds of around EUR 1.1 billion. The second round that we have announced are well on the way in the preparation. We cannot talk about more details there, but it is the divestments of the fertilizer business of Borealis, as well as Slovenian filling station business. Now when it comes to third package, this will be decided then according to our needs for further increasing headroom for possible new steps that we'll decide on later in this year. There are no acquisitions planned for 2021. And also, this is a perspective that we keep with very high discipline. There will be continued changes in our portfolio. And that will also keep on going. And that is what is the third package around that we will announce later in the second half of this year.

Question by **Matthew Lofting – JPMorgan:**
On deleveraging, just wondering the extent to which strengthened macro conditions, oil above 60, strong performance from Borealis and the framework you gave around disposals is increasing your conviction or confidence in delivering sub 30% net debt-to-equity by year-end?

Answer by **Reinhard Florey**:
Matt, regarding deleveraging. Of course, your comment or question makes me happy because also I feel that it will be a little bit easier for us now with this clearly better economic environment to reach the tough target of 30% gearing that we have announced and that we are fully committed to. Now why I'm saying that? First of all, we are keeping a clear discipline on our CAPEX with the EUR 2.7 billion. We will not go beyond that. The question why I'm still hesitating to say we are going sub 30% this year is simply that it's not entirely possible to forecast when the cash inflows from the second row of divestments will come, whether with our commitment to sign them still in this year, whether also the closing will be possible, I cannot fully commit today. So therefore, at least, I would say, the 1.1 billion of the 3 divestments of the first round will definitely come in, and for the second ones, we'll see whether one or the other will also close still this year, then it might be possible to go sub 30%. Otherwise, I still feel comfortable that we can reach the 30% in 2021 and still reap the fruits from the divestments in 2022, also from the cash side. Don't forget, 30% is our target level, so I feel already at 30% more comfortable as I was feeling with 41% when we had the Borealis deal done in 2020. I think we are on a very good trajectory. As I said, around 32%, including the EUR 1.1 billion already after Q1, and we'll continue this journey.

Exploration & Production

Realized natural gas price

Question by **Matthew Lofting – JPMorgan:**
Congrats on a strong performance in Q1. First, on the upstream side, I think the average net gas realization sort of moved higher sequentially to about EUR 10.5 per megawatt hour Q1 average. But as I recall, quite a high proportion of your hub volumes are lagged in terms of the pricing, particularly through Russia and parts of Asia. So could you talk a bit about the outlook for gas realizations Q2 and beyond factoring in those lags?

Answer by **Rainer Seele**:
All right. Matt, I'm more than happy to answer gas question. As you know, I grew up as a pipeliner, therefore, I like your gas questions. Concerning the prices, you can see our guidance is that the realized gas price will be above EUR 11 per megawatt hour. You are right, we have locked in, I think, a EUR 10.4 per megawatt hour for the first quarter. So you should see a higher realized gas price for the upcoming quarters. The reason is that we do have time lag effects in several contracts. I think it's a 2-month time lag for the gas in Russia. For 50% of the gas, we produce there. So the 50,000 barrels per day gas production, which is indexed to European gas prices is coming with a time lag effect of two months. So the higher gas prices, or the rising gas prices we have seen then in Q1, we will see them now starting to run into our numbers for Q2 onwards. So if you have a time delay in the beginning, you have a positive time lag when the gas prices will go down, of course. So another information is that we also have a time lag effect with our production in Malaysia. And this is even higher, it is four months time lag we do have in our contracts. So we see now the gas prices from December in our gas production in Malaysia, and that's why a further increase in gas prices will be supported by higher prices in Malaysia.

One last comment on the gas price development, I think we are going to see, especially in the 2 summer quarters, more a winter price level than the summer price level we are used to. What you can see on the forward price curve in the market is already EUR 20+ per megawatt hour, which is 3 to 4 times higher than the gas price we have seen last year in the 2 summer quarters. So I would say, especially the gas production should contribute more in the upcoming 3 quarters. The major question, I don't answer, you might have in your head, Matt, is how much above EUR 11 per megawatt hour, the price will be at the end of the year. I'll leave it with you, my friend.

Libya

Question by **Sasikanth Chilukuru – Morgan Stanley**:
If you could provide us an update on the current situation in Libya. What is the current production rate there right now?

Answer by **Rainer Seele**:
Your question on Libya, well, the environment in Libya is pretty stable at the moment. I would say I don't see any need to correct my outlook that I'm going to see a stable production until year-end in Libya. The environment has improved. I have discussed with Hans several times, whether or not we are going to send back our expatriates and our experts into the country. We are not there at the moment, but I would say no reason to have sleepless nights about Libya at the moment.

Growth projects

Question by **Giacomo Romeo– Jefferies**:
First of all, I have to join my colleagues in congratulating you for the excellent results. My first question is whether you can provide an update on the evolution of the commercial discussions in Romania with regards to the terms of the Neptun projects. And just to confirm here, if you are able to reach an FID on this project, does it automatically mean that you will not exercise your option for Achimov 4/5?

Answer by **Rainer Seele**:
Giacomo, let's talk about Neptun a bit. As I said already this morning, we are highly committed to the Neptun project. I think we see some progress now in Romania, especially strong signals from the government that they are ready also to start a parliamentarial approval process for the amendment of the offshore law. I think what I could read in the newspaper is that Romgaz has placed a binding offer for the Exxon shares. What was very important for us that in case Romgaz successfully will take over the 50% share of Exxon, the operatorship will move to OMV Petrom. From our point of view, it was very important that OMV will get the operatorship given our technical background in executing this project. I think we would minimize the technical risk, and we have signed it. And well, we prepare for an FID next year. And then, of course, you are right, then we are going to ask ourselves the question on Achimov 4/5. I reconfirm what I said in our last call, that we prepare for 450,000-500,000 barrels per day max production in 2025. And that's why we have to discuss next year at latest, whether or not we would like to continue with the acquisition of Achimov 4/5. Your analysis is absolutely right.

Divestments in Malaysia

Question by **James Hubbard – Deutsche Bank:**
Selling the 4 oilfields in Malaysia, and obviously, you sold Maari last year, I think. I'm just wondering, what is the overall plan for your Asia upstream position? Is it still seen as core and these this process is just selling the more mature assets? Or are you thinking about maybe what the future of the Asian upstream business is for OMV? And does it need an Asian upstream business at all?

Answer by **Rainer Seele**:
Well James, I'm more than happy to take your Malaysia question. You're absolutely right, our divestment of the oilfields is just in line with our strategy that we would like to divest mature fields. We are not an expert in tail end production. That's the reason why we, at a certain point of time, are stepping out. But we are committed to Malaysia. You can see that we, just this year, took an FID on the Jerun SK408 gas field development, and it will bring in 2024 additional around 25,000 to 30,000 barrels per day for the gas production. Your question is do we need even some Asian upstream production. I would say, as we speak about gas, we are talking about a growing market, we are talking about a very healthy market, we are talking about our upstream position in Malaysia, about a very, very low cost, high competitive production we are going to invest for. We are talking about investment projects with the high rate of return in our calculation. So I have lots of arguments when we talk about upstream production, especially in Asia, and part of our strategy, James, is that OMV moves more and more towards Asia. I would even be more open to think and to discuss whether or not we need so much upstream production in Europe, as the European market, as we talk about the different continental markets is a market with a totally different low potential in oil and gas consumption, whereas we are talking about real big growth markets in Asia.

Refining & Marketing

Refining & Marketing result

Question by **Mehdi Ennebati – Bank of America**:
Sorry, this morning, I haven't been able to connect quite early. So apologies if my questions have already been answered. First one regarding the Refining & Marketing. There has been miss compared to the consensus. I just wanted to know was it more due to the marketing or to the refining? Have you been able to generate relatively strong marketing as usual, or did you see any negative impact here on refining products, which might have affected your margin quite significantly?

Answer by **Reinhard Florey**:
Your first question maybe was whether the effect that is a little bit of a soft result in R&M is coming more from refining or from marketing. What we clearly see is that the refining part has been suffering from lower margins as well as lower utilization. So the main part is clearly due to the situation that we still have had a quite low demand in specifically the jet fuels, the kerosene, which led to lower utilization levels. We're still also suffering here in Europe from major lockdown situations due to the COVID pandemic, which deprives people from their normal human right to mobility. So the individual mobility has been drastically reduced. I think this certainly will also improve. From the marketing side, we are still enjoying very good results from the retail business and also from the gas business. Maybe not in that way, as we have seen in Q4, which was extraordinary high and could balance the situation for Q4 a little bit better than it's possible in Q1, but still very strong business there.

Refining margins

Question by **Mehdi Ennebati – Bank of America**:
And if I may, sorry, last question, can you please tell us about your current refining margin level? Would you say that it is currently improving compared to the first quarter? Or would you say that it remains quite under pressure? Would you say that it is roughly in line with Q1, remaining under pressure? Or would you say that it starts picking up?

Answer by **Rainer Seele**:
Maybe I take your question on the refining margin. We see a recovery of refining margins now in April. The refining margin on average we have seen in Q1 was USD 1.7 per barrel, which was the level of Q4 we have seen last year. Refining margin in April so far is something around USD 2.5 per barrel. So the margin has now improved, but still, we are talking about a margin level where most of the refiners really have no fund to operate their refineries. When I look down the road, let's say why we do see a margin improvement. Looking into the refined products, we see good cracks coming with naphtha and with gasoline. And gasoline cracks even improved in April. So the first half of 2021, the recovery of refining margin is supported by now the starting driving season and especially the naphtha and gasoline cracks. Whereas I think that the refining margin in the second half of this year will be supported by better cracks and middle distillates. The product we have, as a problem at the moment in the market, is diesel. The lowest crack you see in the refined products market is coming with diesel. It's even worse than jet what we have seen. So given the fact that transportation will pick up second half of this year, we think it will be backed by recovery of the stronger cracks in middle distillate second half of this year. So we will move into the USD 3/bbl until year-end. That's my view on the refining margins.

Refinery utilization rate

Question by **Raphael Dubois – Societe Generale**:
On the utilization rate at your refineries. When we look at it, ex Petrobrazi, it was only slightly up compared to the previous quarter despite the turnaround at Schwechat in the last quarter, in Q4/20. You still show a better utilization rate than the European average, but this advantage seems to have been shrinking a bit. Can you maybe explain why that is the case, why you could not keep your 2 refineries in Germany and Austria run as much as before?

Answer by **Rainer Seele**:
Raphael, you're absolutely right in your analysis of our refinery utilization. We have a utilization with the 81% compared to Q4. The reason why we are now meeting the limits is that our flexibility to deal with the very low jet demand in the market is now limiting us with the flexibility, shifting more towards petrochemicals. You have seen that we are now expanding the capacities for ethylene and propylene production in Burghausen, but definitely, this is now the case. As I'm expecting that especially jet demand, or let me say this on my view on refining margins. First of all, we see already a recovery of the refining margin. We have seen an average 1.7 in the first quarter. We are now something around USD 2.5/bbl in April. The refining margins are backed now first half on high naphtha and gasoline cracks. The problem we see right now in the markets are the very low cracks of diesel and jet. And diesel is even worse if you look into the cracks than jet. So we have a big diesel problem in the market. And if I look into April, the picture hasn't changed. The picture only has changed towards the better in gasoline as we are going to prepare for the driving season. The second half of this year, I'm expecting a further recovery of the refining margins as we are going to see a better situation in the middle distillates market. So the second half will be supported by the middle distillates, whereas the first half were supported by gasoline. And that's the reason why we are expecting to see a higher utilization second half of this year than first half because of the problems we see additional problems we see with the diesel in the market.

Chemicals & Materials

Chemical margins

Question by **Sasikanth Chilukuru – Morgan Stanley**:
Regarding your guidance for the polyolefin margins. I was just wondering if you could contextualize your guidance for these margins with respect to the margins you've seen in the first quarter, what would substantially higher than 2020 levels translate when you were to compare it with Q1/21 levels and with regards to that, what margin levels are you currently seeing in April in both in Europe and Asia?

Answer by **Rainer Seele**:
Sasi, as we speak about the Chemicals & Materials business, I can confirm that we continue to see good polymer margins in Europe and in Asia. The margins in Europe are a bit higher than in Asia. As the prices, if you look into the prices, the prices in Europe are higher at the moment than in Asia. Maybe the U.S. impact is a bit stronger in Europe than in Asia. I haven't elaborated so much, but that's more or less the situation. What we see is, right, that the olefin margins are continuing to improve into the second quarter. So we might see a shift from polymers to olefins. You might see that in the combination, especially also in the future, that we do have a hedge between the monomers and the polymers, not 100%, but there will be a shift between these 2 business units.

Question by **Raphael Dubois – Societe Generale**:
You have strongly benefited from the non-specialty part of your production in the first quarter. Can you tell us if the specialty part of your production will also see an increase in margins, maybe to reflect somewhat the very strong environment we're in going into the rest of the year?

Answer by **Reinhard Florey**:
Yes, Raphael, you asked about the share of non-specialty or specialty regarding Borealis margins. It is true that with the prices spiking in the polyolefin area, of course, the non-specialty business participated and benefited earlier and higher, and we indicated that already in advance that this would be the case. However, we will see that there is certainly a certain peaking of these prices going on, and that we will see for the non-specialty part, maybe even a slight decrease of these prices in the second half. This is not what we would be expecting in the specialty part. So in the share between specialties and non-specialties, we would see rather again a pickup of the share of specialties in Borealis results. Overall, very strong industrial positions. And be aware that not all the contracts and all the sales are just long-term contracts in the specialty part, but we also have areas where, on a quarterly basis, prices are being renewed. So I'm expecting rather a stronger specialty contribution, specifically in the second quarter now.

Question by **Henri Patricot – UBS**:
Just following up on the previous comments that were made. Just wondering how quickly you captured the higher benchmark petchem margins in Borealis. And you mentioned, in some cases, you have quarterly pricing for specialty. But on the non-specialty side, you said that you kind of fully captured the higher benchmark margins in the first quarter, we should expect to see a bit more of that benefit in the second quarter?

Answer by **Reinhard Florey**:
Sure, Henri. Regarding the petchem margins, I think that we can expect still a very strong second quarter for Borealis. The hike of the margins came continuously over the month. And I don't think that the level that is reached today can be compared to the average of what we have seen in the quarter. So in general, we are expecting both in the non-specialty, as well as in the specialty, a slight increase in the average, but we have to see how the end of this quarter develops towards summer and how these pricing goes. But in general, we are quite, I would say, positive on the development of petchem also for the second quarter.

Inventory effects

Question by **James Hubbard – Deutsche Bank:**
So Borealis result boosted by inventory effects. Can you say anything about the scale of what those inventory gains are and are they broken out anywhere?

Answer by **Reinhard Florey**:
James, regarding inventory effect of Borealis, yes, I think it's important to talk about it because for the other business, R&M, we are showing CCS effects which give you the indication. We don't do that for Chemicals & Materials because in chemical industry, the market does not know CCS logic in that sense. The inventory effect that we have seen in the first quarter is slightly below EUR 100 million. So this should give you a good indication for the Borealis. If you would compare quarter-on-quarter, it would be around EUR 130 million difference because there was a negative effect on the side last quarter, whereas we have a quite sizable effect positive in this quarter.

Question by **Bertrand Hodée – Kepler Chevreux**:
One follow-up question on the inventory effect disclosure. As you mentioned, cash flow was extremely strong, ex working capital, but you benefited from an inventory effect, quite significant. And if I understand well, you did not intend to disclose the inventory effect at Borealis going forward, even if you give us the answer during this conference call. But can you confirm that you won't disclose on, I would say, in your excel supplement or in the press release, this inventory effect at Borealis, which could be from one quarter to another quarter, quite a significant, I would say, delta to assess either your operating results performance or your cash flow performance?

Answer by **Reinhard Florey**:
Yes. Bertrand, I think it's a fair question. Let me put it like that. We are reporting this and to giving you this explicit answer because it has been a very extraordinary effect. Of course, we would love to see many more quarters where we have such a strong spike of prices because if we are talking inventory effect, we are talking much less of a volume effect. It's much more the pricing effect that we see in inventories that more or less came in when they were bought at lower prices, but then, of course, when being sold we are seeing that the value has increased through this pricing. So therefore, I don't think that it's necessary to keep that as a permanent number that we disclosed. But whenever there are extraordinary effects, we will not hesitate to give you the numbers also for comparison from quarter-to-quarter. So if we do not report this as a special topic, then you can confirm that or be confident that the effects are marginal in comparison to the quarters that we compare with.

Question by **Mehdi Ennebati – Bank of America**:
The other question that I have is more for the analysts in order to help us to model. Would it be possible, please, for you to provide regular every quarter, the inventory valuation change effect at the chemicals division, please? Just for us to help us to clean the figures if we want to.

Answer by **Reinhard Florey**:
I think I pointed it in my last answer regarding the inventory valuation to the fact that we have answered this question in this quarter was very clearly due to the situation that we have an extraordinary situation, which we not expect to continue or to repeat every quarter. So I understand that you would like to see a little bit what's the equivalent of the CCS that we have for our R&M situation also for C&M, segment, we will see how appropriate logic that is also in line with the way how the market in general is reporting for chemicals can be applied. But for the moment, we leave it to say when there are extraordinary effects, we will be transparent about them. If we are not saying anything like that, you can rely that there has not been a major effect that's necessary to mention.

Borouge

Question by **Sasikanth Chilukuru – Morgan Stanley**:
Regarding the cash distribution policy or dividend policy for Borouge. If you could remind us what that was. Is it fair to assume a pickup in Borouge net income levels to translate to a pickup in the dividends received from that JV? Or are there any other considerations that I should be aware of in terms of the cash contribution of that JV.

Answer by **Reinhard Florey**:
Regarding the cash distribution of Borouge, first of all, it's important to understand that there is a cash distribution as dividend every quarter. So it's not only a first quarter effect, but we'll see every quarter a dividend from Borouge. Regarding the policy itself, of course, there is no specific disclosure to be done. However, you can definitely count on a rich dividend policy that Borouge is running, which we have been demonstrating over the past quarters. It's also not to be expected that with further investments also in Borouge that dividends would seize. So there is enough potential for leverage also of the company so that there is a continued dividend, maybe not at the same level that we see today, but clearly, continued dividend to be expected.

Baystar

Question by **Henri Patricot – UBS**:
Can you give us an update on Baystar and the new units, the cracker, which I believe was started up in April, whether there's any impact from the Baystar and what you expect in terms of a ramp-up there?

Answer by **Reinhard Florey**:
Henri, on Baystar, I can say that our polymer production is back in the JV, so given this blizzard impact we have seen at the Gulf Coast, we are now back with production of polymers. The cracker, the execution of our investment project was not negatively impacted so far. We can keep the time line, and we are expecting that the cracker will come on stream second quarter of this year.

Circular economy

Question by **Giacomo Romeo– Jefferies**:
You mentioned a few times your efforts on recycling projects. Can you provide a little bit of an outlook of where you see capacity going in the next few years? And how do you see returns evolving in these applications?

Answer by **Reinhard Florey**:
Yes. Giacomo, regarding the recycling project, we are talking several initiatives that are currently being started in OMV regarding the circular economy. One is certainly around our chemical recycling regarding ReOil. And there, the next step that we are planning to still take as an FID this year, is what we call second stage or demonstration plant, where we are leveraging up more or less the pilot plant that we are currently having up and running also on a continuous basis, producing synthetic crude oil that we can input in our refineries that we are taking that up to a production between 15,000 and 20,000 tons per annum for the years to come. This is more or less in between step that we see to demonstrate both the technical, but as well also the economic feasibility and also in preparation of the whole feedstock pipeline and feedstock supply chain that we need. When we have set that up, we would then go into the next step, and we're estimating that this takes place still before 2024-2025 to a full industrial scale which is in the magnitude

of up to 200,000 tons per annum. And those plants then would be even scalable or multipliable on different sites, so that there is also not only one site like Schwechat being benefiting from that, but other plants in Scandinavia, but even in Middle East, could be following suit.

The second stage there is mechanical recycling. And I think Rainer has mentioned it in his speech already, Borealis is taking real efforts there to have not only plans but really concrete projects, both in Sweden as well as in Germany. And there, we are really producing recycled, high density polyethylene, low density polyethylene, but also recycled polypropylene. And those are projects that can deliver directly also in following industries with green products. All of them are first-stage projects, which means smaller scale but fully suitable production for industrial use. And with those also then yielding profitability, there is expansion in this field also planned for the future.

Fertilizer business

Question by **Thomas Adolff – Credit Suisse**:
If I may, just on the fertilizer business that you are looking to sell you said during the pre-marketing space, just kind of want to get a sense for feedback you've had so far, the interest level.

Answer by **Rainer Seele**:
When we talk about the fertilizers, pre-marketing the first reaction is, there is a good interest in the market. What helps, Thomas, is that the business environment for fertilizers has improved. So the appetite, especially if you are on the sunny side of the street, you're more looking around buying some ice creams. And that's happening now in the market. So the improving and better market environment in fertilizers is helping us in the process. So the first reaction is a good one, but it's too early to really give you a more precise indication. Reinhard?