OMV Q3 2023 Conference Call – Q&A Transcript

October 31, 2023

OMV published its results for Q3 2023 on October 31, 2023. The investor and analyst conference call was broadcast as a live audio– webcast at 11:30 am CET. Below is the transcript of the question and answer session, by topic, edited for clarity.

OMV Group

Taxes

Question by **Henri Patricot – UBS:**
I wanted to ask about the cash tax payments, with better cash flow generation than underlying earnings this quarter, looks like it's attributed to some of the extraordinary taxes including the solidarity contribution. Can you remind us what we should expect in terms of cash tax payments over the next few quarters in particular when it comes to these solidarity contributions?

Answer by **Reinhard Florey**:
You have seen that cash tax rate as such has come down from Q2 to Q3. The main impact of course is lesser payments in Norway. Due to the different price levels in Q1 and Q2, we had still payments, referring to the price levels of 2022. That has eased out now. We will not see those kind of impacts anymore in Q4 this year and we are also not expecting this to reoccur in 2024 as the prices overall specifically for gas have come down significantly. Please note that in Q3, we also had less taxes paid than booked in an amount of roughly EUR 150 mn, that's part of our other adjustments that you have seen here. This is normally the deferral of some periods of the payments that you have. So I'm just mentioning that to you. And on the other hand, we have this solidarity contribution in Romania and Austria, together around some EUR 100 mn for Q3. And this has not been paid out as they always are due for payment only in the consecutive year. But of course, they have been booked. This has been around EUR 75 mn for Romania and the rest for Austria.

When you were looking at the outlook for that, of course, it's very hard to predict. In Q4, we would see that the level of tax rate probably stays in the same range as we have seen in Q3, as we are not expecting too much of a difference in the commodity prices, which are the main drivers actually for the tax rate. And in next year, let's see, we don't expect for the beginning of the year a major change, maybe we'll see if there is a cold winter some of the gas prices going up a little bit. But other than that we are not expecting any special topics here.

When it comes to solidarity tax payments, we expect in Q4 the payments to be slightly lesser than in Q3. However, for 2024 there is not any of those taxes to be booked expected, so we will just pay the taxes for 2023. But for 2024, there is no basis in the EU to prolong this and we do not have any indication that this would be the case.

Chemicals & Materials

Potential combination of Borealis & Borouge

Question by **Henri Patricot – UBS**:
I was hoping you could give us a bit of an update on the Borealis, Borouge potential combination if there is anything new you can say around timeline, etc.

Answer by **Alfred Stern**:
We are effectively in negotiations with ADNOC to negotiate a potential combination of Borealis and Borouge. On the industrial logic, we would do something like this because that combination would provide for a growth platform that would also be one of the leading polyolefins companies globally. And we could build on a long-term partnership with our partner ADNOC there to then continue to grow this.

What we are aiming for is an equal share, equal rights partnership in a company that will also be stock listed. Now we are in the middle of these negotiations, and hence cannot make any detailed comments on the progress of those. But of course, we are aiming for the best possible outcome for OMV in these negotiations.

Question by **Bertrand Hodee – Kepler Cheuvreux:**
Coming back on the negotiation with ADNOC and the potential combination between Borouge and Borealis, in parallel ADNOC is also in negotiation with Covestro. Are you involved in those negotiations, because I struggle to understand how you cannot be involved in some way because at the end of the day, should ADNOC buy Covestro, ADNOC may also want to potentially integrate Covestro into the Borouge, Borealis combination.

Answer by **Alfred Stern:**
I want to go back because I think I didn't say it or explain it properly. The discussion that OMV and ADNOC are having at the moment is about a combined polyolefin company. So it will be a focused company that would be aiming to become a leading player in the polyolefin market, so polyethylene and polypropylene with that scope. Covestro does not produce any of these polyolefins. And as OMV, we are not involved in these discussions, and I can therefore also not comment on unrelated business discussions.

Market environment

Question by **Michele Della Vigna – Goldman Sachs:**
Given your unique position in the chemical value chain to see what's going on in the global economy at the moment, I was wondering if you could comment on whether you're seeing any specific areas with signs of life and recovery. And on the other side, if there are some areas that are showing a slowdown versus what we've seen year-to-date?

Answer by **Alfred Stern**:
Around the chemical market, that is of course a little bit more complicated, as we see a very mixed kind of bag of different indications. As you may remember through Borealis, we have a portfolio where we are looking at about 45% of the sales volumes being specialty type of polymers that go into higher value applications and the rest going more into productivity, more commoditized areas. And we see a different type of behavior in those different areas.

Throughout the last couple of months, we have seen on the specialty area good robust demand in automotive, we have also seen good demand in wire and cable insulations, and we have seen weaker demand around the more commoditized areas. I don't know if this is an indication for the future. But what we encountered in the third quarter is that we were able to increase our sales volumes also in the productivity area ensuring high utilization rates of our assets. In particular in Borouge, we have seen versus a year ago that they were able to increase their sales volume quite dramatically. Of course, the comparison is difficult because a year ago, there was still some lockdown restrictions in China.

So compared to the industry, we are able to run high utilization rates in our assets where we see more pressure still is on the pricing side, where we have seen that this is now kind of flattening out, but still a difficult environment. Some progress in being able to move volumes, but still a difficult environment.

Question by **Sasikanth Chilukuru – Morgan Stanley:**
Regarding the polyolefin markets, you highlighted the persistence of structural overcapacity and weak demand. Looking into next year, I was wondering if you could provide some color on how you see the dynamics changing from a supply perspective? Whether you see an overall increase in the supply capacity? If yes, whether it was possible to quantify it and provide some color on where you're seeing these increases? Or will it likely stay flat? Just wanted to check, if we should expect the utilization rates of the European plants to remain low in early 2024 as well.

Answer by **Alfred Stern:**
We have seen in the last couple of years significant capacity additions, and with the current low demand situation that leads to overall low capacity utilization, which is creating the situation as it is. I want to relate this more to a OMV perspective and look how that can affect us.

We have worked hard to make sure that we have well positioned crackers and with this then also polyolefin plants on the different cost curves. Borouge of course, is a very big part of that based on ethane crackers with advantaged feedstock cost we are supplying into Asia with differentiated technology, differentiated products. That leaves us in a good position to also make sure, we can run high capacity utilization. The Baystar polyethylene plant that Borealis just brought on stream, there we will have to do some work in the next couple of months, to fully ramp it up and to then further high-grade the product portfolio. But again that cracker is of course positioned very well taking advantage of US ethane prices that are significantly advantaged.

And finally in Europe on our Nordic crackers, we have invested a lot in feedstock flexibility. In Sweden for example, we're even bringing over ethane from the US to use that cost advantage. And with this, we can also have higher utilization rates. So that's one lever that we will pull. And of course, we also see that the products that we make are demanded in the market, and we will see over time the growth picking up again.

And then on the specialty side, I think this is where we make a significant part of our margin. As I mentioned before, there we see more differentiation, and we of course, need to see how the economy continues to develop. But one area that is our highest margin contributor in specialties is around wire and cable insulations. I really think there we have a long-term growth perspective also driven by the energy transition and transformation that we see globally.

Question by **Bertrand Hodee – Kepler Cheuvreux:**
And then when I look at the chemicals outlook, I see another strong oil demand growth in China, led by mainly petchem feedstock i.e. naphtha and LPG suggesting that there is again, as it was in 2023, very strong petrochemicals capacity addition. In China, it looks like this is still the case in 2024. So do you really expect any improvement in chemicals next year?

Answer by **Alfred Stern:**
I would want to say here that our strategy in that polyolefin area is, that we are focusing on well-positioned assets from a feedstock perspective to have a cost advantage, but at the same time to make sure that through innovation and technology, we continue to grow our specialty portfolio. In total, we are looking at differentiated products that are not aiming exactly for the commodity type of market in order to make sure that we remain then in a competitive position. At this point, I do not want to comment for too long a perspective, but I would agree that fourth quarter and first quarter next year will continue to be difficult quarters. But in the long run, we do see that demand will pick back up and the supply-demand situation will then improve again.

M&A

Question by **Sasikanth Chilukuru – Morgan Stanley:**
Related to M&A, just wondering, are you currently actively looking to acquire more in the chemical space, if you could comment on your appetite for deals beyond the potential Borealis, Borouge combination that would be helpful as well.

Answer by **Alfred Stern:**
I would want to say that we are of course fully focused and in the process at the moment to try forward our discussions together with ADNOC on a potential combination of Borouge and Borealis. And we want to make sure to optimize here the results for OMV and to drive it forward as quickly as possible. Beyond this, we have always said that if we can find ways how to accelerate our transformation, we will also consider inorganic investments. But at this point, I have nothing specific I can report to you there.

Baystar JV

Question by **Irene Himona – Societe Generale:**
On the Baystar JV, you referred to the continuing operational challenges. Are these the normal, let's say, snagging issues with all startups or is it something more fundamental? And does the JV have a clear timeline for resolving them and eventually ramping up to full capacity?

Answer by **Alfred Stern:**
Just for your recollection what was built there was 1 mn t ethane to ethylene cracker, and 625 kt Borstar polyethylene plant. The joint venture already had before two polyethylene plants, so that it now makes a fully integrated 1 mn t ethane to ethylene to polyethylene complex.

Starting up such a complex always takes some time and always faces some issues that need to be resolved, some changes that need to be made in order to make sure everything is running. Those are very complex plants.

I want to mention, maybe two things that you should understand. Number one is that because this is part of a fairly sophisticated and large ethylene network in Texas, it means that the polyethylene plants and the cracker can run in a way independent from each other. That means not if one is shut down, the other one needs to shutdown too. So this is rather helpful in order to mitigate some of the effects.

And then on the timeline, I'd say there's of course a good plan how to resolve the issues that are there. There are some issues that are purely start-up related and making sure we are running all the things properly, but there are also some issues that will take a few months to completely resolve. Of course, there is a good and solid plan for it, and that is not constraining in any way that we continue to have a good forward movement with that complex there.

Fuels & Feedstock

Performance

Question by **Ramchandra Kamath – Barclays:**
If I look at refining performance, it was not quite there despite better headline margins and the ADNOC contribution was also lower. Wonder if you could talk a few things about this.

Answer by **Reinhard Florey:**
When it comes to the refining performance, we have to take into account a couple of topics that were relevant in this quarter. First of all, we had in the total F&F not only refining but also retail. And in the retail part, we have seen that there has been, of course, the

lack of the Slovenian retail assets that lowered the business income in general. But we have also seen not as high retail margins as we have seen in the third quarter of last year that were exceptionally high because of a rebound situation from COVID were actually underway.

When it comes to refining as such, we have seen that the refining utilization has been not at its full height. We have seen a refining utilization at 84%,with an improving utilization throughout the quarter. And we have now also some impacts from the turnarounds on the chemical side also coming back to the refinery in Q3. In Q4, there will be none of that. So, we will certainly see a little bit of a rebound of that utilization level on the refineries.

ReOil®

Question by **Irene Himona – Societe Generale:**
On recycling and ReOil®, I wonder from a technological viewpoint, is there some uncertainty or some doubt concerning the ability to effectively scale up that technology to, let's say, world-scale plants?

Answer by **Alfred Stern:**
I would like to highlight that we have been working on this ReOil® technology for over 10 years now. We have a pilot plant in operation in our refinery in Schwechat since more than five years. And that pilot plant is fully integrated in that refinery, it's been running over the last five years. We have made a lot of optimizations, a lot of tests, what are all the different influences that can happen there. And we have in the meantime, over 20,000 operating hours on this plant, so that it's been really tried and tested for many different occurrences.

And at this moment, we are completing the construction of a 16 kt plant, also in the refinery Schwechat to then bring that to the next level. A 16 kt plant, if I compare that globally, that's often a full-scale recycling plant. Our plan for the full scale is 200 kt and we are already planning then to scale that up, but we wanted to take some of the learnings that have occurred in the scale-up now to 16 kt to transfer that.

We have quite a high confidence level, which I think is also reflected by the fact that we have just signed with Wood, an agreement that together we will license that technology globally to other parties. We believe that makes sense because the technology has a lot of potential, but the product that comes out is not a differentiated product, so that we believe this is a good way, how to accelerate the circular transformation for chemical feedstocks.

Energy

Asia-Pacific divestment

Question by **Michele Della Vigna – Goldman Sachs:**
Could give us an update on the potential divestment of your Malaysian assets? And what you think the timeline could be there?

Answer by **Alfred Stern:**
We are following the process as we have communicated it earlier. We have now received bids for these assets, and we are in the middle of the evaluation of these bids. And we'll then make some decisions in the coming weeks before the end of the year.

Gas Marketing & Power

Question by **Ramchandra Kamath – Barclays:**
Regarding the contribution from the Gas & Marketing business, which is less in this quarter. I understand there was some provision, which negatively impacted margins. But how do you see it going forward into the fourth quarter?

Answer by **Reinhard Florey:**
Yes, indeed there have been two impacts on the gas side. One was that, due to the high level of storage, and on the other hand dropping prices, there have been some impairments of gas inventories in the magnitude of EUR 60 mn. And in addition, you may have seen there has been a mark-to-market adjustment of the contracts with the pipeline capacities, that's pipeline capacity contracts for the next five years in the magnitude of EUR 80 mn. This is simply a mark-to-market valuation, it does not take into account that of course this will be profitable business, when the volumes ultimately will be used and will be sold, else we wouldn't do it. So those are some special effects that you have seen and that lowered the income in general, both on the gas side as well as on the F&F side for this month.

You were looking into an outlook specifically also on the gas trading business. I think the gas trading business always depends a little bit on the weather. We have high storage levels, which allow us of course to take care of all the needs and demands when winter kicks in, and when there is increased trading activity. So we actually are certainly in a situation, seasonally where it's rather an uplift Q4/Q1 in the gas trading results and gas trading business.

Question by **Matt Lofting – J.P. Morgan:**
On Gas Marketing & Power within the upstream or energy business as you now call it, the contribution there seemed probably lower than expectations in the third quarter even accounting for the provisioning effect within the West business. Can you talk about some of the moving parts within that and how you see that looking forward into next year?

Answer by **Reinhard Florey:**
When it comes to Gas Marketing & Power, I have mentioned that there have been some one-time effects going against our result in Q3. However, in general, there is a certain seasonality in the business, specifically the gas marketing.

In Q2 and Q3, we normally have a business where the storages get empty and are being refilled again. So normally strongest quarters are Q1 and the beginning of Q2, but also the ending of Q4 if winter kicks in early. So therefore, the one time effect apart, we have to live with this seasonality, and we do not see any kind of change in the business model as such. And the fact that OMV has some of the largest storages in Europe certainly helps the stability of this business.

Question by **Tamas Pletser – Erste Group Bank:**
Regarding your exposure to the potential disagreement between Russia and Ukraine on the gas transit by Ukraine can you just elaborate, how does it affect your business if this relationship breaks down completely and there is no Russian gas transit from the end of 2024?

Answer by **Alfred Stern**:
At OMV, we have two supply contracts with Gazprom, one is in Germany and one is in Austria. The German gas contract has not had any supply since about the middle of last year. The Austrian gas contract had a lot of uncertainty and variability in the second half of last year and still in January. Since then, Gazprom has supplied the contractually agreed quantities through that period.

Now the Austrian contract is supplied through that pipeline going through Ukraine and Slovakia to the Austrian border. But what we have done in OMV now, over the last 18 months is, we have worked very hard to diversify our supply portfolio, and we have booked logistic capacities, so that today, we are in a position that we can supply all our customer obligations from non-Russian supply sources with the pipeline capacity bookings that we have made, whenever it's necessary also if the Russian supplies would stop. So from this perspective, we can switch the supply then to alternative suppliers.

Question by **Tamas Pletser – Erste Group Bank:**
Do I understand correctly that, is it more like a price risk for you than a supply volume risk. Is it a correct assumption?

Answer by **Reinhard Florey:**
No, as we are always in a hub environment, the prices are not advantaged if they come from Russia or from Norway or from where else. So, the situation is rather to say, how do we deal with all the capacities that we need to bring the gas from places like the Netherlands, Italy, Germany or Norway into the area of Austria and the neighboring countries? But the pipeline capacities are booked also on a long-term basis, so the diversification of the gas supply for our customers has more or less fully happened. So in terms of now interruption that would not change.

Fiscal stability Romania

Question by **Matt Lofting – J.P. Morgan:**
I wanted to just ask you about your perspectives on the fiscal stability that Petrom faces in Romania, in the context of the changes on future concession to the royalty rates that you highlighted earlier in the call. And then also, recent suggestions that some elements of the offshore law pertaining to Neptun, could be up to sort of further discussion as well. So, can you talk about that and the rate of change around that and the extent to which you're comfortable on the fiscal framework and mechanism that Petrom faces going into 2024 and beyond?

Answer by **Reinhard Florey:**
Regarding the Neptun project, everything is stable and no impact at all from these discussions about new concessions because the concession is there, and the concession is untouched from any kind of new activities there. Also, for most of our other production in Romania, we have the concessions in place, and only in a couple of years from now there would be necessary renewal of these kind of concessions. And only by then an eventual change could come in, and there the magnitude also is by far not very exciting to talk about.

So the Neptun part absolutely stable. And when you refer to offshore law discussions, those are just discussions about potential export opportunities that might come on top of what we have, but the project is based on the existing opportunities, and therefore we see that this is a very profitable investment.

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