Inside Conoco Phillips: Last Quarter's Progress

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This past quarter reminded us of the principles which Conoco Phillips lives by: have the "cheapest" oil and gas resources possible (industry term: low cost of supply); and grow free cash flow (available for dividends and share buybacks) as much as possible.

As a pure exploration and production oil company, meaning it doesn't include refining in its business, Conoco's finances are directly linked to the price of oil and gas. This means there is no hedge against lower oil prices, but also no limit to the upside of higher oil prices. Because of this, for years Conoco's management has valued low cost of supply. It constantly assesses its assets and sells the higher cost assets if they no longer fit its cost framework, and if other cheaper assets can be bought. Oil prices softened over the past quarter as OPEC began bringing production back on, and some of Conoco's competitors have announced plans to cut back on production due to softer prices. Conoco has decades of oil reserves at a cost of under $40 per barrel. Management made it clear in the earnings call that at today's $60 oil price, Conoco doesn't need to lower any production plans. At $60 oil, it is still highly profitable in all of its "oil patches" around the world, due to its long-standing insistence on operating only where the cost of production is very low.

CEO Ryan Lance referred to the "have and the have nots" in the oil industry. The "haves", like Conoco, have more flexibility in business operations at any given oil price. Conoco has chosen to cut half a billion dollars from its capital spending program for the year due to oil's weakness. This money is mostly from operating efficiencies and cutting back on discretionary spending. It doesn't affect production and only serves to increase cash flow in this environment.

> *"Free cash flow growth and returns on capital are our North Star. Production growth is just the output of our plan".   –CEO Ryan Lance*

Conoco has a few large projects coming online in the 2026 to 2029 timeframe, on which it's spent a lot of capital for years. (Starting up new projects is always costly.) Fairly soon, though, that capital spending will drop off as the projects start up, further increasing cash flows over the next several years. Conoco's goal is returning 45% of cash from operations to shareholders through dividends and buybacks, and it has delivered on that goal for years. We are confident that Conoco will continue executing its plan well, leading to higher returns for us shareholders in the coming years.