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OXY.N - Q2 2022 Occidental Petroleum Corp Earnings Call

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OVERVIEW:

Co. reported 2Q22 reported profit of $3.47 per diluted share and adjusted profit of $3.16 per diluted share.

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PRESENTATION

Operator

Good afternoon, and welcome to Occidental's Second Quarter 2022 Earnings Conference Call. (Operator Instructions) Please note, this event is being recorded. I would now like to turn the conference over to Jeff Alvarez, Vice President of Investor Relations. Please go ahead.

Jeff Alvarez - *Occidental Petroleum Corporation - VP of IR*

Thank you, Jason. Good afternoon everyone, and thank you for participating in Occidental's Second Quarter 2022 Conference Call. On the call with us today are Vicki Hollub, President and Chief Executive Officer; Rob Peterson, Senior Vice President and Chief Financial Officer; and Richard Jackson, President, Operations, U.S. Onshore Resources and Carbon Management.

This afternoon, we will refer to slides available on the Investors section of our website. The presentation includes a cautionary statement on Slide 2 regarding forward-looking statements that will be made on the call this afternoon.

I'll now turn the call over to Vicki. Vicki, please go ahead.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Thank you, Jeff, and good afternoon, everyone. We achieved a significant milestone in the second quarter as we completed our near-term debt reduction goal and activated our share repurchase program. At the beginning of this year, we established a near-term goal of repaying an additional $5 billion of debt, before further increasing the amount of cash allocated to shareholder returns. The debt we completed in May brought the total debt repaid this year to over $8 billion, surpassing our target at a quicker pace than we had originally anticipated. With our near-term debt reduction goal accomplished, we initiated our $3 billion share repurchase program in the second quarter and have already repurchased more than $1.1 billion of shares.

The additional allocation of cash to shareholders marks a meaningful progression of our cash flow priorities as we have primarily allocated free cash flow to debt reduction over the last few years. Our efforts to improve the balance sheet remain ongoing, but our deleveraging process has reached a stage where our focus is expanding to go to additional cash flow priorities.

This afternoon, I'll cover the next phase of our shareholder return framework and second quarter operational performance. Rob will cover our financial results as well as our updated guidance, which includes an increase in our full year guidance for OxyChem.

Starting with our shareholder return framework. Our ability to consistently deliver outstanding operational results, combined with our focus to improve our balance sheet, have positioned us to increase the amount of capital returned to shareholders. Considering current commodity price expectations, we expect to repurchase a total of $3 billion of shares and reduce gross debt to the high teens by the end of this year. Once we have completed the $3 billion share repurchase program and reduced our debt to the high teens, we intend to continue returning capital to shareholders in 2023 through a common dividend that is sustainable at $40 WTI as well as through an active share repurchase program. The progress we are making in lowering interest payments through debt reduction, combined with managing the number of shares outstanding, will enhance the sustainability of our dividend and position us to increase our common dividend at the appropriate time. While we expect future dividend increases to be gradual and meaningful, we do not anticipate the dividend returning to its prior peak.

Given our focus on returning capital to shareholders, it is possible that we may reach a point next year where we've returned over $4 per share to common shareholders over a trailing 12-month period. Reaching and maintaining returns to common shareholders above this threshold will require us to begin redeeming their preferred equity concurrently with returning additional cash to common shareholders.

I want to be clear about 2 things. First, reaching the $4 per share threshold is the potential outcome of our shareholder return framework, not a specific target. Second, if we begin redeeming the preferred equity, this does not mean there is a cap on returns to common shareholders as cash would continue to be returned to common shareholders above $4 per share.

In the second quarter, we generated $4.2 billion of free cash flow before working capital, our highest quarterly free cash flow to date. Our business has all performed well, and we delivered production from continuing operations of approximately 1.1 million BOE per day, in line with the midpoint of our guidance and with total company-wide spending of capital of $972 million.

OxyChem reported record earnings for the fourth consecutive quarter with EBIT of $800 million, as the business continued to benefit from robust pricing and demand in the caustic, chlorine, and PVC markets. Last quarter, we highlighted the Responsible Care and Facility Safety Awards that OxyChem received from the American Chemistry Council.

OxyChem's accomplishments continue to be acknowledged. In May, the U.S. Department of Energy honored OxyChem as a Better Practice Award winner, which recognizes companies for innovative and industry-leading accomplishments in energy management. OxyChem received the recognition for incorporating an engineering, training and development program that led to process changes, resulting in energy savings that reduced CO_2 emissions by 7,000 metric tons annually. It's achievements like this that make me so proud to announce the modernization and expansion of one of OxyChem's key plants, which we'll detail in just a minute.

Turning to oil and gas. I'd like to congratulate the Gulf of Mexico team in celebrating first oil from the new discovery field, Horn Mountain West. The new field was successfully tied back to the Horn Mountain SPAR using a 3.5-mile dual flow line. The project came in on budget and more than 3 months ahead of schedule. The Horn Mountain West tieback is expected to eventually add approximately 30,000 barrels of oil production per day and is an excellent example of our ability to leverage our assets and technical expertise to bring new production online in a capital-efficient manner.

I'd also like to congratulate our Al Hosn and Oman teams. Al Hosn achieved a recent production record following the first full plant shutdown as a part of a planned turnaround in the first quarter. Oxy's Oman team celebrated a record high daily production at Oman North Block 9, which has been operated by Oxy since 1984. Even after almost 40 years, Block 9 is still breaking records with strong base production and new development wedge performance, supported by a successful exploration program.

We have also been active in capturing opportunities to leverage our deep inventory of U.S. onshore assets. When we announced our Midland Basin JV with EcoPetrol in 2019, I mentioned how excited we were to be working with one of our strongest and longest-standing strategic partners. The JV has worked exceptionally well for both partners, with Oxy benefiting from incremental production and cash flow from the Midland Basin with minimal investment. We are fortunate to collaborate with a partner who has extensive expertise and with whom we share a long-term vision. This is why I'm equally excited this morning to announce that Oxy and EcoPetrol have agreed to enhance our JV in the Midland Basin and expand our partnership to cover approximately 20,000 net acres in the Delaware Basin. This includes 17,000 acres in the Texas Delaware that will utilize WES' infrastructure.

And in the Midland Basin, Oxy will benefit from the opportunity to continue development with an extension to the capital carry through the end of this agreement in the first quarter of 2025. In the Delaware Basin, we have the opportunity to bring forward the development of high-quality acreage that was further out in our development plans, while benefiting from an additional capital carry of up to 75%. In exchange for the carried capital, EcoPetrol will earn a percentage of the working interest in the JV asset.

Last month, we reached an agreement with Sonatrach in Algeria to enter into a new 25-year production-sharing agreement that will roll Oxy's existing licenses into a single agreement. The new production-sharing agreement renews and deepens our partnership with Sonatrach, while providing Oxy with the opportunity to add reserves and continue developing a low-decline cash-generating asset with long-standing partners.

Even with 2022 expected to be a record year for OxyChem, we see a unique opportunity to expand OxyChem's future earnings and cash flow generating capabilities by investing in a high-return project. On our fourth quarter call, we mentioned a FEED study to explore the modernization of certain Gulf Coast chlor-alkali assets and diaphragm to membrane technology. I'm pleased to announce our Battleground plant, which is adjacent to Houston Ship Channel in Deer Park, Texas, is one of the sites that we will modernize. Battleground is Oxy's largest chlorine and caustic soda production facility with ready access to both domestic and international markets.

The project is being undertaken in part to respond to customer demand for chlorine, chlorine derivatives, and certain grades of caustic soda that we can produce with newer technology. It will also result in increased capacities for both products. The project is expected to increase cash flow through improved margins and higher product volumes, while lowering the energy intensity of the products produced. The modernization and expansion project will commence in 2023, with a capital investment of up to $1.1 billion, spread over 3 years.

During construction, existing operations are expected to continue as normal, with the improvements expected to be realized in 2026. The expansion is not a prospective build as we have structurally advanced contracts and internal derivative production to consume the incremental chlorine volume, while caustic volumes will be contracted by the time the new capacity comes online.

The Battleground project represents the first sizable investment we've made in OxyChem since the construction and completion of the 4CPE plant and ethylene cracker that were completed in 2017. This high-return project is just one of several opportunities we have to grow OxyChem's cash flow over the next few years. We are conducting similar FEED studies for additional chlor-alkali assets and plan to communicate the results when complete.

I'll now turn the call over to Rob, who will walk you through our second quarter results and guidance.

Robert L. Peterson - *Occidental Petroleum Corporation - Senior VP & CFO*

Thank you, Vicki, and good afternoon. In the second quarter, our profitability remained strong, and we generated a record level of free cash flow. We announced an adjusted profit of $3.16 per diluted share and a reported profit of $3.47 per diluted share, with the difference between the two numbers primarily driven by gains in early debt extinguishment and positive mark-to-market adjustments.

We were pleased to be able to allocate cash to share repurchases in the second quarter. To date, we have repurchased over 18 million shares as of Monday, August 1, for approximately $1.1 billion for a weighted average price below $60 per share.

Also, during the quarter, approximately 3.1 million publicly traded warrants were exercised, bringing the total number exercised to almost 4.4 million with 111.5 million remaining outstanding. As we said, when the warrants were issued in 2020, the cash proceeds received will be applied towards share repurchases to mitigate potential dilution to common shareholders.

As Vicki mentioned, we are excited to enhance and expand our relationship with EcoPetrol in the Permian Basin. The JV amendment closed in the second quarter with an effective date of January 1, 2022. To maximize this opportunity, we intended to add an additional rig late in the year to support the JV development activity in the Delaware Basin. The additional activity is not expected to add any production until 2023, as the first Delaware JV wells will not come online until next year.

Similarly, the JV amendment is not expected to have any meaningful impact on our capital budget this year. We expect the Delaware JV and the enhanced Midland JV and to allow us to maintain or even lower industry-leading capital intensity in the Permian from 2023 onwards. We will provide further details when we provide 2023 production guidance.

Given the January 1, 2022 effective date and related working interest transferred to our JV partner in the Midland Basin, we have adjusted our full year Permian production guidance down slightly. Separately, we are reallocating a portion of the capital we earmarked for OBO spending this year to our operated Permian assets. Reallocating capital operating activity will provide more certainty in our wedge delivery for the second half of 2022 and the start of 2023, while also delivering superior returns given our inventory quality and cost control. While the timing of this change has a slight impact on our 2022 production due to activity relocation in the second half of the year, the benefit of developing resources that we operate is expected to result in even stronger financial performance going forward. The updated activity slide in the earnings presentation appendix reflects this change.

The shift in OBO capital, combined with the JV working interest transfer, as well as various short-term operability matters all contributed to us slightly lowering our full year Permian production guidance. The operability impacts are primarily related to third-party issues, such as downstream gas processing interruptions in our EOR assets and other unplanned disruptions at third parties. For 2022, company-wide full year production guidance remains unchanged, as the Permian adjustment is fully offset by high production in the Rockies and the Gulf of Mexico.

Finally, we note that our Permian production delivery remains very strong, with a growth of approximately 100,000 BOE per day when comparing the fourth quarter of 2021 through our implied production guidance for the fourth quarter of 2022. We expect production in the second half of 2022 to average approximately 1.2 million BOE per day, which is notably higher than the first half of the year. Higher production in the second half of the year has always been an expected outcome of our 2022 plan, in part due to ramp-up activities and scheduled turnarounds in the first quarter.

Company-wide third quarter production guidance includes continued growth in the Permian, but considers the potential for tropical weather impacts in the Gulf of Mexico combined with third-party downtime, and production decline in Rockies given our lower activity set as a result of relocating a rig to the Permian.

Our full year capital budget remains unchanged. But as I mentioned in our previous call, we expect capital spending to come in near the high end of our range of $3.9 billion to $4.3 billion. Certain areas that we operate in, especially the Permian, continue to experience higher inflationary pressures than others. To support activity into 2023 and address the regional impact of inflation, we are reallocating $200 million of capital to the Permian. We believe our company-wide capital budget is sized appropriately to execute our 2022 plan, as the additional capital for the Permian will be reallocated from other assets that have been able to generate higher-than-expected capital savings.

We are raising our full year domestic operating expense guidance to $8.50 per BOE, which accounts for higher-than-expected labor and energy costs, primarily in the Permian, as well as continued upward pricing pressure on our WTI index CO_2 purchase contracts in the EOR business.

OxyChem continues to perform well, and we have raised our full year guidance to reflect the exceptional second quarter performance as well as a slightly better than previously expected second half of the year. We still see the potential for market conditions to dampen from where we are today due to inflationary pressures, though the long-term fundamentals continue to remain supportive, and we expect third and fourth quarters to be strong by historical standards.

Turning back to financial items. In September, we intend to settle $275 million of notional interest rate swaps. The net liability, or cash outflow required to settle these swaps, will be around $100 million at the current interest rate curve. Last quarter, I mentioned that as WTI averages $90 per barrel in 2022, we would expect to pay approximately $600 million in U.S. federal cash taxes. Oil prices continue to remain strong, increasing the possibility that WTI may average an even higher price for the year. If WTI average $100 in 2022, we would expect to pay approximately $1.2 billion in U.S. federal cash taxes.

As Vicki mentioned, year-to-date, we repaid approximately $8.1 billion of debt, including $4.8 billion in the second quarter, exceeding our near-term goals of paying $5 billion in principal this year. We have also made meaningful progress towards our medium-term goal of reducing gross debt to the high teens. We began repurchasing shares in the second quarter, further advancing our shareholder return framework as part of our commitment to return more cash to shareholders. We intend to continue allocating free cash flow towards the share repurchases until we complete our current $3 billion program.

During this period, we will continue to view debt retirement opportunistically and we'll likely retire debt concurrently with share repurchases. Once our initial share repurchase program is complete, we intend to allocate free cash flow towards reducing the face value of debt to the high teens, which we believe will accelerate our return to investment grade. When we reach this stage, we intend to reduce the emphasis of our allocation of free cash flow from primarily reducing debt by including additional items in our cash flow priorities.

We continue to make incremental progress towards achieving our goal of returning to investment grade. Since our last earnings call, Fitch assigned a positive outlook to our credit ratings. All three of the major credit rating agencies rate our debt as one notch below investment grade, with Moody's and Fitch having assigned positive outlooks. Over time, we intend to maintain mid-cycle leverage at approximately 1 times debt-to-EBITDA, or below $15 billion. We believe this level of leverage will be appropriate for our capital structure as it will enhance our equity returns while strengthening our ability to return capital to shareholders throughout the commodity cycle.

I'll now turn the call back over to Vicki.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

We're now prepared to take your calls.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from John Royall from JP Morgan.

John Macalister Royall - *JP Morgan Chase & Co, Research Division - Analyst*

So can you talk about the various moving pieces in the CapEx guidance? I know that you raised the Permian number, but kept the total the same. So what are the areas that were the source of funds for that raise? And then any early look into some of the moving pieces for next year with this new FID for Chems and then the change in structure with EcoPetrol? Just anything you can give us on kind of the puts and takes going into next year would be helpful.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

I'll let Richard cover the changes in the CapEx, and then I'll follow up with the additional part of that question.

Richard A. Jackson - *Occidental Petroleum Corporation - SVP*

John, this is Richard. Yes, so a few moving pieces as we look across the U.S. onshore. And as we look at it, a couple of things occurred during the year. I think, first, from an OBO perspective, we had a wedge assumed in our production plan. And early in the year, that became a bit slower in terms of delivery. And so we went ahead and made the move to reallocate some of that capital into our operated, which did a few things.

One, it secured that production wedge for us, but it also added resources for the back half of the year to give us some continuity on the back half of the year. We like that we did that. As Rob mentioned in his comments, these are high-return projects that are very good. So that was a good move. And then securing some of those resources early in the year in terms of rigs and frac core has played out well in terms of our timing to manage inflation and improve performance as we hit this ramp-up for the back half of the year.

The other piece of that, so step 2 is really reallocation from Oxy. And so part of that is coming from LCV. We can talk in more detail on that if we need to. But that's really -- as we hit the back half of the year, we look to be coming in closer to midpoint for low carbon ventures. That's really just more certainty around the direct air capture development in some of the CCUS hub work that we've got in place. And so that, plus, I think, some other savings around the rest of Oxy, really contributed to that balance.

So if you think about that extra [200], I'd say 50% of that is really around activity adds. So we were a bit front-end loaded in our plan for the year. That allows us to take that capital and keep continuity, especially across drilling rigs, which will give us optionality as we go into 2023.

And then the other piece is really around inflation. We've seen that pressure on that. We've been able to mitigate a large piece of that. But we've outlooked an additional 7% to 10% sort of outlook compared to plan on the year. We've been able to again make up an incremental 4% of that in operation savings. So pleased with the progress against that. But we did start to see some inflationary pressures come up. And so that capital helps address that uncertainty, I would call it, for the rest of the year.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

I would say, on capital for 2023, it's still way too early for us to determine what that would be. But the EcoPetrol JV would fit into the Resources allocation, and will compete with the capital within that program.

John Macalister Royall - *JP Morgan Chase & Co, Research Division - Analyst*

Okay. Great. And then switching over to chemicals. If you guys could just talk a little bit about the fundamentals in that business. Coming off a very strong 2Q, but a big step down in guidance for the second half. So if you could just give some color on the source of the strength in 2Q and what you see changing in the second half?

Robert L. Peterson - *Occidental Petroleum Corporation - Senior VP & CFO*

Sure, John. I would say conditions in both the vinyls and caustic soda business that are largely the ones that determine how we perform overall in Chemicals. They were obviously very favorable in the second quarter. And when we see both conditions -- both businesses at favorable points, you have the significant earnings impact leading to the record performance we had in the second quarter.

If you go into the third quarter, I would say, the extreme tightness that we've been experiencing for quite some time in the vinyls business has become more manageable. And that's really from improved supply and some softening in the domestic market, while conditions in the caustic soda business remain very strong and continue to improve. I would say the macroeconomic conditions are still indicative that when you look at interest rates, housing starts, GDP, they're kind of trading unfavorably, which is why we talked about a softer second half relative to the first half. But we're also entering a very unpredictable time of the year being the latter part of the third quarter here in terms of weather, which can certainly upset supply or demand either way. And so it's very difficult to look out very far as we enter the very beginning of the hurricane season or the peak of hurricane season.

And the other thing I would say that has impacted the business a bit that we're trying to incorporate into the outlook is the Chinese shutdowns related to COVID, sort of the no COVID tolerance policies is backing up their demand in terms of needs for chemicals and pushing other Asian chemicals into other parts of the world, including impacting exports from the U.S. And so there's a bit of a softening there effect. But again, these are all things that can be modified relatively in a short basis if something were to change in either of those.

But because of that, macroeconomic trends and our normal seasonal declines you would see in the fourth quarter in the business, we are projecting a softer second half of the year after the first half of the year. But again, what we're projecting is quite strong by historical standards. Even the guidance for the third quarter as it is now would have been historically a decent year in many years for the Chemicals business, let alone a quarter.

Overall, when we look at business on PVC, we're still seeing growth year-over-year. Domestic demand is up almost 6% through June. And PVC demand, including exports from the U.S., total demand is up about 4.5%. The chlorine side of the business, we're still seeing growth of 3% to 4% this year. All the market structures remain strong. There's still a lot of pent-up demand, as you can imagine, coming off of the last two years. But those are all areas in durable goods, et cetera, where we can see impact from interest rates, inflation, disposable income, et cetera. So again, part of it is just trying to forecast what that might look like, doing the same thing everyone else is doing right now, trying to gauge the depth of a potential recession and the impact on demand. But overall, still very favorable conditions in the business, but just not as favorable as they were in the second quarter.

Operator

The next question is from RaphaÃ«l DuBois from Societe Generale.

Raphaël DuBois - *Societe Generale Cross Asset Research - Equity Analyst*

The first one is related to Algeria. Now that you have signed this 25-year contract extension, I was wondering if you could maybe give us some better color on what is the production potential for Algeria and whether there is a change in the mix between liquids and gas that we should be expecting?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Currently, under the agreement that we signed, we're still -- we'll be producing basically oil production with associated gas. And primarily from the fields we've already been developing just expanding those out. So I'd say that from the standpoint of our production outlook, currently it's going to look a little bit lower next year than it looks this year because of the structure of the contract. But our cash flow is going to be approximately the same. So it's just based on the terms. And we have a lot of potential, we believe, in the existing fields to continue to develop those out. So the remaining reserves that we'll be able to add as a result of just the contract extension will be about 100 million barrels.

Other than that, there's a lot of potential for further evaluation. So we've included the 3D seismic survey as a part of the evaluation, so that we can start to better increase our recoveries from those conventional fields because they're all relatively low decline and supported with gas injection and potentially ultimately some CO_2 injection.

Gas is not a part of what we're developing over there yet, but could be in the future, should there be an opportunity for us to find it commercially competitive with the other projects that we have internally.

Raphaël DuBois - *Societe Generale Cross Asset Research - Equity Analyst*

Great. And my follow-on question would be about chemicals. This Battleground CapEx project that you have announced, you said earlier that you would have more plans that you will consider for modernization. When could we hear about the next one to be modernized? And could you maybe remind us of the capacity of Battleground so that we can have a feel for the CapEx intensity of such project and what we could be expecting going forward for other projects.

Robert L. Peterson - *Occidental Petroleum Corporation - Senior VP & CFO*

Sure, Raphael. So we have talked about potential conversions beyond the Battleground project. So at this point, we've made the decision to move forward with the Battleground conversion. As indicated in the remarks, we will continue to operate the facility throughout the construction process. There may be some short periods where we'd take very short outages for important connections between existing infrastructure in the facility. We're confident, throughout that process, we can build inventory and continue to build product with no impact on our customers. And so as you think about the Battleground process, you should not assume any loss of sales or margin during the actual project itself.

So when you look at the other facilities, once we convert the Battleground facility, we already have membrane technology and polyramix, which is a non-asbestos type diaphragm technology, at our Wichita and Geismar facilities. And we're in the process right now of making a conversion change at our Taft facility to polyramix. So the announced project, that will not only convert Battleground but increase its capacity by 80%, will only leave our Convent and Ingleside facilities utilizing asbestos diaphragms. And we'll begin the conversion studies on those as we get further underway with the actual Battleground conversion. We'll do them sort of in series together. We won't wait for one to be completed to make a decision on the other, but we'll sort of stagger them together. But obviously, what we're going to do with those facilities isn't as pertinent as to moving forward the Battleground project right now.

And so from a capital intensity standpoint, we don't provide individual capacities of our facilities. But what I would say though is that the amount -- cost of $1.1 billion that we've included in the slide deck, I would not use that as a proxy necessarily that -- for the other two facilities. The facilities are all individually unique, not only from different sizes and capacities of the facilities, but they all have different equipment associated inside and outside battery limits. They have different conversions that will go along with them.

In addition that, at this stage, as we mentioned, the Battleground facility expansion is determined also with existing contractual obligations we've secured for the chlorine side of the business, the derivative side of the business moving into the project. We're not expanding the project, hoping to get additional demand for those molecules are already sold in the future. At this time, we don't have needs to expand either our Convent facility or Ingleside facility. So at this stage, if we were to proceed with an FID decision on one of those, it would simply be a conversion of process change. And so it would be difficult to take that and I certainly wouldn't multiply that number times three and come up with a number for those other two projects to be included in that.

And so as we get further along with the Battleground project, we'll start sharing ideas on subsequent changes in the future. But at this time, the only decision we made is to actually move forward with the Battleground one.

Jeff Alvarez - *Occidental Petroleum Corporation - VP of IR*

Raphael, this is Jeff. I'd add one thing to what Rob said. The EBITDA number we've provided would be, the way I'd look at that is more of a mid-cycle EBITDA, not at current pricing or current market conditions. So you can use that for your estimates.

Operator

The next question comes from Devin McDermott from Morgan Stanley.

Devin J. McDermott - *Morgan Stanley, Research Division - VP, Commodity Strategist for Power Markets & Equity Analyst of Power and Utilities Research Team*

So I wanted to ask on Low Carbon Ventures. One of the moving pieces in the cap guidance this year was LCV spend coming in toward the midpoint. I was wondering if you could just talk a little bit more broadly about the progress you've been making towards some of the milestones that you set forth earlier this year. And as part of that, the Inflation Reduction Act that's recently been introduced has some supportive language in there for carbon capture and also direct air capture. So can you talk about if that were to move forward, how that might impact the cadence of investment over the next few years?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Devin, I'll start, and then pass it over to Richard. And while we're on the Inflation Reduction Act, I just want to cover a little bit more about what's in there. There's a lot of things in there, ranges from alternative fuels to renewable energy, EVs, hydrogen, methane, emission reduction and carbon capture use and sequestration. But some of the things that impact us are the -- on federal land, oil and gas royalty rates increasing, increased minimum bid rates for leases, increases in annual rental rates, but not excessively, and increasing bond requirements, also offshore royalty rate increases. And one of the good things is that it does require oil and gas lease sales ahead of granting right of ways to wind and solar. It requires royalties in oil and gas produced, whatever it's used for, unless it's flared for safety reasons or used for the benefit of the lease.

But one of the interesting things about the act is that it reinstates the Lease Sale 257 from the Gulf of Mexico, in which we had gotten some key leases. And so that's really important for us as a company. The other thing is that it requires the resumption of the scheduled lease sales for the GoM from 2017 to 2022.

And with respect to carbon capture, which is probably the most impactful to us, is there are a lot of things around the enhancement to 45Q. And when you look at the Gulf of Mexico benefit to us and you look at the requirements for the methane emissions and emission reductions and that sort of thing, which are things we already were doing, this is turning into for us a net very positive bill should it get passed.

So I'll turn it over to Richard, so he can give you a little more color on what the CCUS enhancements are.

Richard A. Jackson - *Occidental Petroleum Corporation - SVP*

Yes. Devin, let me start with just a few kind of progress points on both our direct air capture and CCUS, and then get a couple of specifics on, like Vicki said, how this can potentially help our development plans.

I think from direct air capture, the critical pieces are continuing to move well. I think from a technology and engineering standpoint, we were able to finish FEED. We're on track and plan to begin construction by the end of this year. And we're really taking that FEED and working hard on putting together specific bid packages and being very thoughtful about the supply chain behind that as we go into the end of the year. So we're spending time with that.

From a market support, continue to have very strong support from the carbon dioxide removals in terms of the sequestered CO2 offtakes. And so continue to see good movement on that. Obviously, the policy support couples with that to help really backstop our development plan. And then in terms of capitalization, as we continue to de-risk, we are thoughtful on how to think about capitalization not only for plant one but beyond and continue to see and know that those partnerships will be meaningful.

And so really, on that piece, for the end of the year, again, looking to start construction, finish detailed engineering and then work our innovation work streams. We've got our innovation center with Carbon Engineering going, seeing really good progress there, lots of pieces in learning, again, for plant one. But I think one of the things we picked up in that facility is really thinking about how do you continue to reduce the cost to capture for the life of a plant. And so it provides lots of opportunity for that.

Just briefly on the CCUS hubs, we continue on our three really focused areas on the Gulf Coast. We've been able to secure now over 100,000-acre target for pore space development. Very pleased with that. Lots of great engagement with emitters. And then we had the announcements, I think we picked up on the last quarter with our midstream partnerships to be able to retrofit or think about moving that CO2 efficiently within those hubs. So that goes well, expect more updates on both of those as we go into the year. Lots of dynamics, I'd say, over the last quarter. And so we'll put that into plans for 2023 and beyond that we'll communicate.

So just lastly on the -- in terms of some of the policy that plays our way. I think for us, we think about that, we communicated it in our LCV update. It's really an acceleration capability for us. It gives certainty in some of the revenue to allow us to build this development, which is good because the important part of making this business work is really on us. We've got to improve the technology. We've got to lower the cost, and we've got to develop our manufacturing and project development success.

And so having certainty to be able to accelerate that development plan, we believe, allows us to reduce those costs quicker and it creates a sustainable business sooner. And so when you look at both a business and emissions reduction over the next several years, we think this could be very meaningful. Longer runway to be able to develop that scale is contemplated in the language. Obviously, increased value support, that aligns with a lot of CCUS work done collectively around the world to kind of pick what needs to happen to create this catalyst. And so very thoughtful alignment there.

And then the final thing is, I think importantly, recognition for all sources. So point source from industrial or power sector emissions, but carbon removals and direct air capture specifically recognized. And then for the collective CCUS community, recognition of small and large sources, I think is important. And so they were very inclusive to capture both the small and large. And that's good for us and what we're doing, but that's good for other developers. And so I think it really does create the economies of scale that we hope and plan for to make this commercially successful.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

And just to conclude on that, I'd say that the federal leasing, onshore, offshore, the methane emission reductions and carbon capture, while we talked about what it does for Oxy, this is very good for our industry. Lots of companies will benefit from this. It will provide jobs and it will help the country meet the goals that the President has set out for emission reduction.

Devin J. McDermott - *Morgan Stanley, Research Division - VP, Commodity Strategist for Power Markets & Equity Analyst of Power and Utilities Research Team*

A lot of positives to look forward to there. My second question is just on inflation. You mentioned in the prepared remarks that you've been able to take some steps to offset inflationary pressure. I was wondering if you could talk a little bit more on the underlying inflationary trends and also the offset initiatives that you have in place?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Yes. We had originally assumed $250 million based on our 2020 actuals, that incremental of $250 million this year. Our current assessment is $350 million to $450 million. And unfortunately, for Richard, it's all falling in his area. But they're dealing with it very well. I'll pass it to him to give you the details.

Richard A. Jackson - *Occidental Petroleum Corporation - SVP*

Yes. Perfect. Thanks, Vicki. Yes, just to walk through that, I mean, a couple of things. Certainly, we have seen that 7% to 10% incrementally for us this year. But in our base plan, we had assumed a 2% offset, and we're now up to 6%. And so part of our strategy, and I'll talk through a couple of pieces on this whole thing, was securing quality resources.

If we get into the production cadence for the second half of the year, that delivery schedule and performance is very important. And so working with the right vendors to secure that has been important for us. But let me just rattle off a few. Like most people, OCTG has seen some of the highest sort of inflationary pressures. We work with one key supplier and one distributor for that. And so when we think about sort of inflation, you think about what is the supply security and then what is the pricing. In the supply security, we feel good out a year and really have worked that hard over this year. Developing in core areas like we do gives us a lot of ability to do that. And in pricing, we secure out about six months. And so we feel good going into the end of the year and then into 2023, that we're timing that fairly well in terms of how that looks.

Rigs and frac core, as I mentioned earlier, securing some of those operated resources. Shifting the OBO dollars allowed us to get in front of that and get, again, the right rigs and frac cores for that. We're contracted with a little over 50% of our rigs through the first part of next year. And our frac core's similar as we look out. And so feel good about that, but we've really narrowed again to the core frac and rig providers that we feel like can secure performance.

And then finally sand, again, we've worked a lot on that. I think, one, we've gone to more integrated frac providers, and they continue to help us on logistics and sand supply. But then our sand supplier, our logistics facility in Aventine has allowed us to get ahead on that. And so we feel like supply is secured, and most of our price is secured through the second half of the year. So those have been the big areas that have moved up for us. It has definitely been drilling and completion focused, facilities has seen a lot less, 5%, OpEx a lot less as well. So hopefully, that provides some detail in terms of what we've been doing.

Operator

The next question comes from Doug Leggate from Bank of America.

Douglas George Blyth Leggate - *BofA Securities, Research Division - MD and Head of US Oil & Gas Equity Research*

Vicki or Rob, I wonder if I could go back to the discussion around potentially being a bit more aggressive than a $4 cash return in 2023? And I guess my question is, where do you see the, I guess, the flexibility regarding trying to pay down the preferred burden, I guess, the $10 billion, versus continuing to pay down debt? What's the trade-off between those 2, if you could try and frame it for us? I guess I'm trying to understand how much more than $4 per share you'd be prepared to go?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Doug, it really depends on the macro. Right now, we're really trying to -- we can't even forecast from one hour to the next or even one minute to the next what prices are going to be. So a lot of our strategy around the preferred would depend on the macro because of -- as you know, the terms of the deal are challenging if not planned out in a way that enables you to take advantage of the trigger point. So currently, we're really trying to assess what the macro will look like, and we're going to be prepared to make the best value decision, whether that's continued debt reduction along with preferred and along with common.

But right now, the reality is that from our capital framework, we have always had a priority to reduce debt. We'll continue to do that. And we'll do that at a faster pace than the maturities. We just don't know how fast we'll do it. And with respect to the preferred, it really depends on what we see getting through the end of this year and looking into next year what the macro will be, whether the recession, if there is one, will be short or long or deep, and what the other opportunities may look like from a debt perspective, and that could depend on what inflation does.

Douglas George Blyth Leggate - *BofA Securities, Research Division - MD and Head of US Oil & Gas Equity Research*

I appreciate the answer, Vicki. And I'm going to stay with you, if I may, as a quick follow-up. So before things got crazy over the last couple of years, you had talked about low single-digit growth in production. And of course, the priorities all changed with the balance sheet. So as you kind of get line of sight to the balance sheet and back to perhaps where you want it to be, what are you thinking now in terms of what happens to the growth element of prioritizing in terms of where you relatively prioritize capital? And I'll leave it there.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Well, the good thing is what we see that we have today is a great opportunity, and that is that we don't have to grow our cash flow right now. And we have an opportunity because of the valuation of our stock right now to continue to make that a key part of our value proposition going forward. We'll do a little bit of dividend increase. We'll certainly mature our debt faster than what the current schedule is in terms of maturities because we want to accelerate that. But we'll also buy back a significant volume of shares, or at least we hope to over the next few years. And we don't feel the need to grow production until we get beyond that point because we feel like one of the best values right now is investment in our own stock.

Operator

The next question comes from Neal Dingmann from Truist.

Neal David Dingmann - *Truist Securities, Inc., Research Division - MD*

Vicki, maybe just to follow on that last one. On M&A, are you saying that sort of given the current upstream, midstream OxyChem, you'll likely stand pat with either you don't really obviously need to divest anything and still the best spend on the money is to buy stock, would it be fair to say the biggest M&A might be coming from the low carbon area?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Yes, I think that the only M&A that we see that would make sense for us is what we have been doing, and that's just to get bigger in the areas that we are. So increasing our working interest and/or trading acres for bolt-ons to where we are right now in the Resources business and in the EOR business. So we have opportunities to do that. We picked up a little bit offshore. So that's -- those are the kind of M&A.

So we're not talking big M&A here. That's not something that we feel like we need to do. But with respect to Low Carbon Ventures, that is a bit of a different story because we're growing a business there. And the -- what we're doing there is looking for technologies that fit within our strategy and that support our strategy. We're not going to take the shotgun approach, where we're putting dollars into 100 different little small tech companies. We're looking for technologies that make our strategy better. And where we find those, we're going to make equity investments when we feel it's a part of what we want to build ultimately.

I think the team has spent with just about $200 million, they have gotten us into two technologies I really think are revolutionary. One is NetPower, which generates electricity at a fairly low cost, lower than a traditional gas plant with carbon capture. So this -- NetPower technology generates electricity, but also captures the emissions. So there are no emissions and no volatile organics or anything like that. So NetPower is really important for us.

And then direct air capture. Back to NetPower, it's going to be revolutionary, I believe, for the electric power generation industry around the world. So that's the technology that's critically important. Direct air capture is, too. And we're looking at some other technologies. There are a few things that we're putting money into that we believe has a real chance to improve our business. And those are -- that's the way we kind of look at investments and low carbon opportunities.

Neal David Dingmann - *Truist Securities, Inc., Research Division - MD*

Okay. And then one last for either Robert or Jeff maybe. Just on the preferred, has there been any conversation about maybe just direct repurchase of those given obviously the same firm mind. Obviously, a lot of equity in the company. I'm just wondering, is there -- or is that just going to be sort of, I guess, buying back as you would your debt and all?

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

It's really going to be a part of a more comprehensive evaluation as we go forward. So we'll look at that as time passes, and we'll certainly keep you guys updated. But what we intend to do is make the best value decision and proceed with the capital framework that we've laid out.

Operator

The next question comes from Jeanine Wai from Barclays.

Jeanine Wai - *Barclays Bank PLC, Research Division - Research Analyst*

Our first question, I guess, maybe heading back on cash returns and a follow-up to a couple of the other questions. The plan for 2023-plus now is to retire debt maturities as they come due. We're looking at your debt schedule, and there's really nothing more than like $2 billion coming due in any one year, so super manageable until 2030. You've got cash building on our model to, call it, like $12 billion on strip by the end of the year. So lots of options. You had some helpful comments on the macro governors on how you're going to allocate capital over the next year or 2. Do you have an updated view on your reserve cash level? We realize there's a lot of reasons to hold cash above that, but that's always a helpful number for us.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Yes. Before I pass that to Rob for the answer to that question, I just want to say that you're right about our debt maturities. So we expect this year to be able to lower our debt based on what we see from the macro by another $2 billion to $2.5 billion, which would get us close to $18 billion. Then to get us down to the $15 billion that Rob mentioned in his script is that we would have -- those maturities would come due, all of them, before August, end of August of 2025. We don't want to wait 3 years to get our debt down to $15 billion. So we would expect to, assuming the macro allows, to cut that considerably. We do want to get to the $15 billion sooner rather than later. So we'll fit that in. And that is still a priority for us. I'll pass it to Rob now for the other question.

Robert L. Peterson - *Occidental Petroleum Corporation - Senior VP & CFO*

Yes, Jeanine. And so certainly based on what Vicki just said and the fact we'll target, we should be able to do well beyond $1.9 billion that we have for the balance of the year on the share repurchase program, assuming the macro is consistent or relatively consistent to the strip prices right now. And part of targeting that will be some of the maturities you listed off. So -- but we've been able to opportunistically balance between short- and long-term debt maturities. As we look at what we've done year-to-date, it's about 45% in the current decade, about 55% in later dated notes.. And so we continue to be opportunistic between knocking out near-term maturities, including ones that are higher interest rate coupon ones now because of the way they've come down with interest rates, but also achieving discount on longer-dated bonds. So you can expect that mix to stay together.

As far as cash reserves, certainly with a very manageable debt maturity profile, we've been holding higher cash levels historically. We ended last year about $2.5 billion. I think we'd be comfortable with something closer to $1.5 billion by the end of this year, providing another certainly $1 billion of cash to work with this year just from the reduction on reserves.

Jeanine Wai - *Barclays Bank PLC, Research Division - Research Analyst*

Okay. Great. That's very helpful. Maybe if we could turn to operations and the Permian. You probably provided some really helpful color on the Q3 Permian guide in your prepared remarks. And the implied 4Q Permian guidance calls for, I think we calculated 12% increase quarter-on-quarter to hit the midpoint. And it sounds like from your comments, there are some third-party stuff that's going on that may come back online in Q4, which will help. But any comments that you have around kind of how you try to stack the deck in your favor on execution in Q4 in the Permian, that would be really helpful just because I think a lot of people are looking at the Permian at the end of the year and trying to figure out implications for next year.

Richard A. Jackson - *Occidental Petroleum Corporation - SVP*

Yes. I appreciate it. Walk through a few pieces. You're exactly right was we thought about sort of this building security in our production delivery for the year. There are several pieces that were important to us. If I go back even to where we started and entered the year from a rig count perspective, we've added -- if you go back to second half of '21, we went from about 11.5 rigs to the first half of this year over 15, to second half of the year at 19. And so being able to secure those operated rigs early to get the performance was really important to us.

So same thing in the back half of this year. If I look at first half versus second half, we look to add about 78 more wells online compared to the first half. So a tremendous step-up in activity. We're able to utilize our frac cores more efficiently with the development plans that we've put together. We're adding one additional in the second half of this year, but we're really creating much more smooth operations with what we've done and transition with that OBO capital.

And I guess the pieces I'd point to, what's been important to us operationally is, again, back to performance. Most of the capital for the second half of the year and the production deliveries in the Delaware, we have about 80% of those wells that are coming online are Third Bone Springs to Wolfcamp A. So it de-risks a lot in terms of that production delivery. We've added lateral length. We're 1,000-foot longer compared to last year to when we look at the second half of this year.

Our 24-hour IP is about 14% better than the first half of last year. And so all of that has added in terms of de-risking the second half of the year. Drilling completion efficiencies improved. Our feet per day is up quarter-to-quarter about 10%. Our non-productive time is reduced about 7% in the Delaware. And so what we've seen as we've added these rigs, we've been able to work as an operational team, the performance continues to improve. And we're looking at the second half of the year expecting about a 10% time-to-market improvement with those operations. So put a lot of pieces in place in the first half of this year, now we just need to go execute. But really, the plan has been built to achieve that production growth you noted, and we're well on our way.

Operator

The final question comes from Neil Mehta from Goldman Sachs.

Neil Singhvi Mehta - *Goldman Sachs Group, Inc., Research Division - VP and Integrated Oil & Refining Analyst*

The first question is just the path to investment grade. Can you provide any color in terms of the milestones that you're getting to in order to achieve that? How are -- how should the investment community think about timing recognizing it's out of your control? And what would getting to investment grade mean to your business?

Robert L. Peterson - *Occidental Petroleum Corporation - Senior VP & CFO*

Yes, Neil. Sure. So year-to-date, as we mentioned, we paid $8.1 billion of debt, certainly far beyond the $5 billion initial target we established for the year. And included in that, in the second quarter, we knocked out 60% of what I would call the annual risk associated with our zero coupon bonds that was occurring every October. If you look back to July of last year -- or June of last year, we retired almost $15 billion of debt. So very meaningful progress on the debt reduction side of it.

But in addition to the debt reduction, all three agencies have their own other metrics. I'll call them, the return IG. And so they're all sitting, as we discussed, one notch below. Our forecast that we have internally have us exceeding the majority of these criteria before the end of the year or, in many cases, we're actually ahead of now on the last 12-month basis. But the conversation we've been having with the agencies would suggest, I just want you to get more comfortable, that in a different oil price environment, and all of the agencies have long-term oil prices well below current oil prices, that they would be comfortable that we would not slip back into being a high-yield type credit.

But again, like I said, take something like Moody's, for example, they want to look at retained cash flow to adjusted debt to be greater than 40% and essentially the retained cash flow excludes the preferred dividends. But the adjusted debt does include half of the Berkshire. So the Berkshire does factor into that. And so we're well ahead of that forecast. And even we're adjusting for Moody's price forecast relative to ours.

And in the case of Fitch, I'll give you an example. They also look at our sort of mid-cycle funds flow from operation is just covered 5.5x. The preferred is excluded from the funds flow, but it's included in interest expense. We're going to be well over 5.5x certainly this year by year-end. And so I think on a lot of these statistics, we are passing through these very rapidly, probably much more -- certainly rapidly than we suspected or the agencies suspected. We're having very constructive conversations with them and making sure that the decisions we're making are contributing towards that.

As you said, we don't have ultimate control over when that occurs, but comfortably looking at all of the various metrics that they've thrown at us relative to our financial policy and metrics. I feel confident that we would be in good stead with all those toward the end of the year. We have a gap with S&P's expectations on reported debt, but that's really the only one that we're going to have a significant gap in right now. But certainly with Fitch and Moody's, I'm confidence on those two agencies that what they've laid out for us explicitly on terms of metrics, that we can meet this before the end of the year.

Operator

In the interest of time, this concludes our question-and-answer session. I would like to turn the conference back over to Vicki Hollub for any closing remarks.

Vicki A. Hollub - *Occidental Petroleum Corporation - President, CEO & Director*

Just want to thank you all for your participation in our call today, and have a good day. Thanks.

Operator

Conference has now concluded. Thank you for attending today's presentation. You may now disconnect.
