STL.OL - Q1 2011 Statoil ASA Earnings Presentation

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and welcome to Statoil’s first-quarter earnings presentations and conference call. My name is Hilde Nafstad. I’m the Head of Investor Relations in Statoil.

Before we start, let me say that there are no fire drills planned for today. So in case the fire alarm goes off, you will need to exit through the two doors in the back of each side of the room and continue on towards the same side.

This morning at 7.30 Central European time we announced the results for the first quarter of 2011. The press release regarding the results was distributed through the wires and through Oslo Stock Exchange. The quarterly report and today’s presentation can, as usual, be downloaded from our website, Statoil.com. There is a link directly to the presentation on the front page of Statoil.com.
I will ask you to kindly make special note of the information regarding forward-looking statements, which can be found on the last page of the presentation.

Please note that questions can be posed by means of telephone. Questions cannot be posed directly from the web. The dial-in numbers for posing questions can be found on the website. The operator of the conference call will explain the procedure for posing questions over the phone immediately before the Q&A session starts.

It is now my privilege to introduce our Chief Financial Officer, Torgrim Reitan.

Torgrim Reitan - Statoil ASA - CFO

Thank you, Hilde, and good afternoon, everyone. It is a pleasure for me to present our results for the first quarter 2011, a quarter with very good progress within key areas.

The production has developed as we planned and it is satisfactory in the first quarter. It is in line with my expectations so far. We have had significant progress when it comes to putting new production capacity on stream. Our demonstration plant at Leismer in Canada and the field development Peregrino in Brazil are both on stream currently. Both of these are examples of large developments that are now put into production. And these fields, they are in ramp-up phase and are both long-lived assets. And they will contribute with more than 70,000 barrels per day in new capacity to Statoil.

Furthermore, we have now closed the sales process of selling 40% of both of these assets, which we used to own 100%. And those transactions, those are generating proceeds of more than NOK30b and accounting gains of more than NOK14b. You should please note that it is only the oil sand transaction that is part of the first-quarter results. The Peregrino transaction that was closed in April, and that belongs to the next quarter.

So through these transactions we have demonstrated how we create value. We have applied our North Sea experience and competence to large and complex developments and we have demonstrated value creation through the portfolio optimization. Furthermore we have sanctioned new projects in Norway, in Canada and in Algeria. Vigdis North and Katla in Norway, those are both part of the fast-track portfolio of projects, Hibernia in Canada and the In Salah Southern Field in Algeria.

In February, I told you that we sanctioned 20 projects in 2010 and that we plan to sanction 40 more projects in 2011 and 2012. And this is still valid. And it is good to see that we progress as planned when it comes to project development.

Furthermore, we have had significant success with the Skrugard discovery in the Barents Sea. And this represents a significant progress in the region and it is strengthening our belief in the potential in the Arctic areas. And we are also very satisfied with the awards in the 21st licensing round on the Norwegian Continental Shelf, where we secured new acreage in the Barents Sea, close to the Skrugard discovery. And in addition we had acreage in an interesting part of the Norwegian Sea, actually very close to the Luva discovery.

We have also made a discovery in Brazil. That is close to the Peregrino field. And it’s firming up volumes for further development in this area. And in that area our campaign will continue with further drilling activity.

We have also got drilling permits in Gulf of Mexico. And we are actually the only company that currently holds two drilling permits after the moratorium. And I expect that we will resume our drilling activity soon in that area.

And lastly, I am satisfied that we have accessed new exploration acreage as well in deep water Gulf of Mexico -- excuse me, in deep water in Angola, the pre-salt Angola, and in Kazakhstan through the Heads of Agreement on the Abay block in the Caspian Sea.
So overall I am very satisfied with the strategic progress during the quarter.

Then over to production. Our production this quarter is satisfactory. It is in line with my expectations. However, it is not more than we need to be in line with what we have guided at. The reason for equity production being 6% below first quarter were discussed in February at our capital market update.

And first of all, Gullfaks is currently not producing at full capacity. And this will have an annual or yearly impact of around 30,000 barrels per day. The production at Gullfaks is stabilized. And we have not had negative surprises from the field and its reservoirs. But it is still too early to conclude on when we will increase the production from the Gullfaks field.

I’m also pleased to see that we are bringing new fields on stream in line with what I have told you. And start-up and the initial production from Leismer and Peregrino have been in accordance with what I expected. But I will remind you that they will gradually be building up production and you should not expect to see significant production contributions before we get closer to the end of 2011.

Gas production this quarter has been strong. It has been in line with normal seasonal patterns, although somewhat lower than first quarter 2010. The winter months will normally have significantly higher gas production than the summer months, and this year will be no exception.

As you know, we have reduced production permits related to the fields Ormen Lange and Troll. Both of those fields produced well during the first quarter. And their reduced permits, they will mostly have an impact in the second and the third quarter this year.

All right, then over to the earnings. This quarter we have delivered operating results, the third-largest operating results in Statoil's history. The quarter has been characterized by high oil and gas prices. And our net operating income came in at NOK50.7b. And this is an increase of 28% compared to first quarter last year.

And, as usual, we adjust for certain items in the accounts to make the quarters comparable from an operational point of view. And the NOK3.4b of adjustments in this quarter are mainly related to the partly divestments of our oil sands position, where we booked a gain of more than NOK5.5b. Furthermore, we reversed impairments related to our regas facility, Cove Point in the US. That amounted to NOK1.6b. This was partly offset by an under-lift situation in the quarter and by change in fair value of inventories. As such, we delivered adjusted earnings of NOK47.3b. That is an increase of 22% compared to the same period last year.

Liquid prices increased by 33% and gas prices increased by 20%. And that impacted the accounts with NOK17b in the quarter. Our production was, as expected, lower this quarter and that contributed negatively with NOK5b compared with first quarter last year.

We are stepping up exploration. And our exploration cost increased by NOK0.6b in first quarter compared to last year. And that is mainly related to increased drilling and increased field development costs in the early phase.

Lastly, we see a slight increase in operating expenses and DD&A. And that is due to more fields coming on stream and increased estimates related to abandonment costs.

So the adjusted earnings after tax decreased by 2%. And that is due to a high tax rate on adjusted earnings. This is largely caused by a higher income from the Norwegian upstream activities and consequently higher taxes and higher tax rate on our international activities. And I will come back to tax in more detail in a few minutes.

Then some details on the various segments. After the reorganization of Statoil, we have made some changes to the segment reporting. We do now report on three operating segments in addition to Statoil Fuel & Retail. Development & Production Norway
delivered adjusted earnings before tax of NOK39.4b. That is a 35% increase compared to last year. The increase was mainly due to 33% higher oil prices in krone and 38% higher transfer price of gas between MPR and DPN.

And increased prices contributed with NOK14b in higher revenues compared to last year. This is partly offset by lower year-on-year production of oil and gas and that contributed negatively with NOK3.3b. Furthermore in that segment DD&A increased by NOK1b due to new fields coming on stream and an updated removal and abandonment cost estimate which we have mentioned earlier.

Development & Production International, they delivered an adjusted earnings of NOK5.2b and that is a 16% increase year on year. The increase was mainly due to 33% higher oil prices in krone. And that contributed with NOK3b in increased revenues. This was partly offset by lower equity production due to suspension of production in Libya and lower gas nominations on partner-operated fields internationally. In addition, we have higher exploration expenses. And that was mainly related to expensing of the Kiwi well in Egypt.

Marketing, Processing and Renewables, MPR, as we now call it, they delivered an adjusted earnings of NOK2.7b. And that is a 47% decrease compared to first quarter last year. That decrease, that was mainly due to that the transfer price between MPR and the Norwegian offshore area increased by 38%, while the realized gas price increased less, with 20%.

Furthermore, the contribution from the marketing and trading activities was less in the quarter due to lower margins from more short-term sales. Also the ownership share in Gassled is reduced from 32.1% to 28.5%. That was valid from January 1. And this is in accordance with the ownership agreements that were put in place when Gassled was established 10 years ago.

And lastly, within that segment, there has been a loss in the crude processing, trading and marketing due to weak trading results from trading gas liquids and from lower refining margins.

Okay. Then over to tax. The tax rate on reported results was 68%. Both the gain on the oil sands transaction in Canada and the reversal of impairment at Cove Point have very low tax rates. And this is the main explanations for the difference between tax on the reported results and adjusted earnings.

The tax rate on adjusted earnings also deserves attention this quarter, both because the total tax rate was higher than previously guided, but also because the tax rate in the segments differ from what I normally expect to see. Firstly, the higher share of the earnings derived from Norwegian Continental Shelf where the tax rate is high. And this pulls the average tax rate up. Secondly, the tax rate for development and production Norway is high due to relatively lower effect of the uplift in an environment with high oil prices.

We have, when we invest in Norway, we can from a tax point of view depreciate the assets with 30% in addition to the full investments and that can be done over six years. And the impact of that additional tax value on the margin is less when the oil price is high. The impact of that is less in the totality when the oil price is high. So that is part of the explanation. And you should expect to see a tax rate on Development & Production Norway close to 74% going forward if the current price environment persists.

The tax rate within Development & Production International is impacted by the dry exploration well in Egypt. In Egypt we have no tax shield. We have also had one-off tax adjustments in the International business. And in addition, a relative high share of the income this quarter comes from Angola, from Algeria and from Nigeria. In these countries the tax rate is rather high and around 50%.

We have previously guided on a tax rate internationally around 40% to 45%. However, in the short term you should expect a somewhat higher tax rate within this segment and I expect to see it to be around 50% to 55% for the time being. In a couple of years, when production from Brazil and North America steps up, I expect the tax level to be reduced.
Within the MPR segment, the tax rate is a consequence of the earnings compositions within the segment. And the contribution this quarter is mainly from the natural gas area, where the tax rate is relatively high. And I expect going forward to see a combined MPR tax rate around 70%. But you should expect the tax rate within this segment to have some volatility based on the composition of the earnings, which will vary from quarter to quarter.

Our guiding on the adjusted tax rate on a corporate level has not changed and it remains in the range 70% to 72%. The change in the short-term outlook for tax rates internationally implies that I expect a tax rate towards the upper end of the range for the rest of 2011.

Then over to the cash flow. We had a very strong cash generation in the first quarter, driven by high oil and gas prices, good production, as well as proceeds from sale of assets. The cash flow from our underlying activity amounted to NOK57b in the quarter. We paid NOK16b in tax; that was in February. And the cash flow used in investing activities amounted to a gross investment of NOK19b.

However, the net investments ended at NOK8.7b. That is due to that we adjust from the proceeds from the sales of assets. And that is related mainly to the sale of the stake in the oil sands -- Canadian oil sands business. As a comparison, in the first quarter last year the net investment was NOK19b. So the underlying cash generation for the quarter after investment and taxes was, as such, NOK32b before other financing activities.

For the next quarter, we will have two tax payments, each of approximately NOK14b. In June we will pay approximately NOK20b in dividends. However, the proceeds from the Peregrino transaction is received and sits in our accounts, but they will be part of the next quarter’s cash flow. So you should expect a quarter with large payments in and out.

Then to the balance sheet. The balance sheet continues to be strong and the net debt to capital employed is 19% end of quarter. And that is a reduction from 25% at year end.

Then over to forward-looking statements and guiding. As I said at the start of my presentation, our first-quarter production was in line with my expectation and in line with what we need to meet our guiding, but not more than that. Our view for the rest of the year has not changed and our production guiding therefore remains for 2011 we expect that to be around 2010 level or slightly below.

And I will use the opportunity to remind you on what I said in February. When comparing 2011 with 2010 production, the risk is more on the downside than on the upside. And this is still valid. There is uncertainty related to the new fields ramping up. And we have extensive maintenance program and there will be gas off-take uncertainties. And please note, for the next two quarters seasonal gas off-take and maintenance will leave us with a substantially lower production level than in first quarter.

The winter months will normally have significantly higher gas production than the summer months and this year will be no exception. In fact, the reduced permits for Troll and Ormen Lange will mostly affect the production in the second and third quarter of 2011.

Then maintenance. You might remember that last year was impacted by heavy maintenance for our gas facilities in the third quarter. This year as well we will have maintenance that affects both liquids and gas production. And I expect a maintenance impact of approximately 100,000 barrels per day in the second quarter. Around 70% of this will be related to liquids.

I also expect that the total maintenance impact to be around 50,000 barrels per day over the year. And this is also mainly related to the liquids production. Important things to note is that this year the maintenance will be more evenly spread over the next two quarters than last year.

And my last point on the next two quarters is related to the Norwegian Continental Shelf. You can expect the production from the Norwegian Continental Shelf for second and third quarter in 2011 to be somewhat lower than the total production from
the Norwegian Continental Shelf in the same quarter in 2010, but the NCS production will be more evenly distributed between the quarters this summer.

With regard to exploration activity and organic investments, we maintain the guidance for 2011.

So that concludes my presentation. And thank you very much for your attention. And then I will leave the word to you, Hilde, who will lead us through the Q&A session. Thanks.

QUESTIONS AND ANSWERS

Hilde Nafstad - Statoil ASA - Head of IR

Thank you very much, Torgrim. We will now turn to the Q&A session. And for this session Torgrim will be joined by the Senior Vice President for Accounting and Financial Compliance, Kaare Thomsen. The session will last for approximately 15 minutes. I will ask you to please limit yourself to one question at a time. For the audience in the room, please raise your hand if you have a question. Microphones will be passed and please keep the microphones close to your mouth. Please state your name and your company.

Operator, can you please explain the procedure for asking questions over the telephone?

Operator

(Operator Instructions).

Hilde Nafstad - Statoil ASA - Head of IR

We will first take questions from the audience here in Oslo. Do we have any questions from the room? I cannot see any hands. So I suggest we then turn over to the audio conference audience. Are there any questions, operator?

Operator

Yes. We have three in the queue at this time and we’ll take the first question now. Ladies and gentlemen, please remember to state your name as well as your company name. Here we go.

Oswald Clint - Sanford Bernstein - Analyst

Hi. Oswald Clint here at Sanford Bernstein. I’ll just try two quick ones, please, Torgrim. Firstly, just on upstream OpEx on a unit basis does seem to be up quite substantially, even though you said there was a slight increase in operating cost. It looks to be up 9%, 10%. I wonder if you could just talk about that, what could be the major drivers of that, and that’s on a year-over-year basis.

And the second question, I’m just curious on the reversal on the Cove Point regasification terminal almost 12 months after you actually wrote that down, in terms of why you’re writing back half of that provision from last year. Thank you.
Torgrim Reitan - Statoil ASA - CFO

All right. Thank you. When it comes to unit production cost, there is an increase year on year on that one. It is mainly related to costs related to startup of production. And we are in a period now where we are preparing for a lot of startups. And the startups are coming in later. And one example of that is the Peregrino field that started in April, where we had significant costs in the quarter related to that field to get it on stream. So that is the major part of that explanation.

Going forward, we don't give a specific target on the unit production cost. We see that it is slightly increasing. It is slightly increasing as we go. Not much more than by inflation actually, so it is in that range. What we aim at is to maintain our competitive position when it comes to unit production cost. We are amongst the better companies on benchmarks and we aim to maintain that competitive positions.

Specifically I would like to mention the Norwegian Continental Shelf, where we have fields in a lot of different places. We have some fields that are on decline and have very high unit production cost. We have fields with close to NOK100 per barrel. And we have new fields with significantly lower. And we see that the new fields actually compensates well for the more old fields when it comes to the unit production cost on a Norwegian Continental Shelf level. But you should expect this parameter to increase slightly as the years go by.

When it comes to Cove Point and Cove Point expansion, we did quite some impairments related to that last year. What has happened over the last year is that we renegotiated the capacity related to Cove Point expansion. So that was an explanation of the reversal that we did in -- that was in the fourth quarter.

Cove Point and Cove Point expansion is looked upon as one common asset from an accounting point of view, and related to the Snohvit volumes. We see increased value of diverted cargos away from the US, so the Snohvit cargos are not going to that terminal; they are going other places at significantly higher prices. So the value of that value chain is higher when the spread is high. So that is the main explanation for the reversal of that one. So the value of our LNG value chain is higher now than we expected it to be last quarter.

Oswald Clint - Sanford Bernstein - Analyst

Okay. Thank you.

Hilde Nafstad - Statoil ASA - Head of IR

Next question, please, operator.

Hootan Yazhari - Bank of America-Merrill Lynch - Analyst

Hi, it's Hootan Yazhari from Bank of America Merrill Lynch. A couple of questions. Your gearing has obviously fallen quite dramatically, both the booking of the Canadian asset sale and you're looking to book Peregrino in the second quarter so, again, you should see another substantial drop-off in gearing; can you just give us some color around how management is now considering the gearing level? Are you looking towards acquisitions or shareholder distributions to address what is a very lowly-geared balance sheet?
And, also, just coming back to the cost side, are you now in a period where you feel that all the cost reductions that you were aiming for in your previous targets have been achieved, or do you believe that costs can remain under control and you continue to cut costs and implement initiatives or should we continue to expect costs just to grow in line with inflation? Thank you.

**Torgrim Reitan - Statoil ASA - CFO**

All right, thanks. First, gearing. It is a comfortable situation when it comes to the balance sheet and, as the CFO, it is a good place to be; however, I am -- of course, this is a situation that we monitor closely. The best proposition I can give to you as investors is quite easy; it is actually to realize a great project portfolio that we have in hand. We have more than 100 projects in the pipelines. We are going to sanction 40 more projects over the next two years and we have a lot of things to do in the portfolio.

And those projects actually competed very well in the industry when it comes to breakeven prices, an average breakeven price around $50 per barrel. So that is, to me, the best value proposition I can give and the best way that I can use -- that we can use the money. When that is said, we have an investment program which is at $16b this year and with the current price environment that is -- our gearing is expected to be decreased if that persists.

On your specific comments on M&A, I will of course -- I appreciate the question but I will, of course, not answer that question. What I can say is that our radar screen is large; it has always been. We have been quite actively in the acquisition and divestment market of the last four years to five years so you should expect there to be activity on that, going forward, as well.

When it comes to capital distribution, we have suggested to the Annual General Meeting a dividend of NOK6.25 and that will be paid in June -- early June. And we are also asking the Annual General Meeting for a mandate for share buyback but please remember that is something that we have done for many years so that is just to have the toolbox available as we always want it to be fully loaded. That is the guidance I would like to give along that one.

When it comes to costs and cost reduction, we took out significant synergies after the merger; that is more or less delivered. We, of course, benchmark ourselves heavily towards other companies and other peers when it comes to cost competitiveness; also beyond the unit production cost. We see that we compete well across most perspectives but when that is said we can always be better at costs and that has still a significant focus in the Company.

So, the initiatives that was implemented after the merger, that has been delivered on. We are working constantly on further reductions. For instance, during the financial crisis, we said, okay, we will have to do quite a bit, and we did. And a few examples; we reduced travel costs by, I think it was, 27% in the Company over a year; just one small examples that goes along a lot of categories. But we are working fiercely on further cost improvements, going forward; I think that is important.

**Hilde Nafstad - Statoil ASA - Head of IR**

All right?

**Hootan Yazhari - Bank of America-Merrill Lynch - Analyst**

Yes, thank you.

**Hilde Nafstad - Statoil ASA - Head of IR**

Operator, do we have more questions from the audio please?
Operator
Yes, ma'am. We do, ma'am; we'll take the next one now.

Teodor Nilsen - First Securities - Analyst
Yes, hello. Teodor Nilsen from First Securities. I have two questions. First one is related to the MPR division where you reported pretty weak results compared to consensus estimates at least and you say that's due to difficult trading market and low natural gas margins, so my question is how is the outlook for this division?

Second question is related to the Peregrino South discovery that you announced April 14; is this a potential tie-in candidate to the current installation and what is the volume potential of this discovery? Thank you.

Torgrim Reitan - Statoil ASA - CFO
All right, thanks. MPR results and the question what do we expect, going forward? There are some stable elements of that results; it's the results from the Gassled and the transport and processing part; that will typically be a stable part of the results. The refining business will fluctuate with refining margins from quarter to quarter. And then it comes to the more commercial units and they will typically also fluctuate depending on the market opportunities as they arise. It is hard to give a guidance on the level; you should expect it to fluctuate. I would say that last quarter is not very good results from the trading activities but it is expected to fluctuate.

Just to give some flavors on the main drivers of the natural gas trading results. The prices on the national balancing point was increasing quite rapidly through the quarter. We have always a lot of gas at hand that we need to sell and we cannot sell it on the day-ahead basis, and so on, so we need to be in front of the market. We sell gas before we actually get to the day when we have to deliver it so that is --- there's a lagging effect in the results on the gas, while the internal price between the upstream business is an average of the prices noted in the market in the period, so that explains part of it.

On the oil side, it was especially linked to one of the products, a strategy which was very profitable last year and this quarter it has impacted negatively on that strategy. But that strategy, in whole, is providing value. So that just exemplifies that the results will fluctuate, dependent on the market circumstances.

When it comes to Peregrino South, I am enthusiastic about it. We reached 130-meter column of hydrocarbons. We have not stated volumes related to it and -- so I'm not prepared to do that currently but it proves that the area where we have Peregrino is an exciting one. It has potential beyond the Peregrino field and it serves as, as you know, firming up volumes that we expect some day will be produced.

Hilde Nafstad - Statoil ASA - Head of IR
Thank you. Next question, operator.

Operator
Yes, ma'am. Here we go.
Barry MacCarthy - Royal Bank of Scotland - Analyst

Good afternoon. It’s Barry MacCarthy from Royal Bank of Scotland here. Thank you for the presentation. I have a question on slide seven on the cash flow. You show the cash flow from underlying operations NOK57b; taxes paid takes NOK16b off that, can you help me reconcile that, please? With the stated cash flows provided by operating activities on page 32 of the release which are NOK30b for the quarter, and there's some large moving items in working capital section and the largest -- among the largest the increase in the current financial investments; if you could help me understand that then that would be great. Thank you.

Torgrim Reitan - Statoil ASA - CFO

All right, thanks. I'll leave the word to Kaare Thomsen which -- to answer that question.

Kaare Thomsen - Statoil ASA - SVP for Accounting and Financial Compliance

Yes, I think you referred to page 32 of the financial review, which starts with a NOK50.3b cash flow from operating activities and what we have done is adjusted for our next part which is called adjustments to reconcile to net income to cash flows provided by operating activities, the depreciation, the exploration and the FX and the sale of assets, and that's altogether net NOK6.4b; that takes the NOK6.4b and the NOK40.23b up to NOK56.7b.

When you ask about the cash flow from operation, I also want to emphasize that, for accounting purposes, the changes to financial investments and derivatives is an operational part of the cash flow but it's really, for us, part of the liquidity. What's placed in the market between over and above three months is not cash and cash equivalent anymore; it's on the operations. So, the build-up -- the change there of NOK13.2b is not really from a commercial point operation; it's the financial deposits which we make in the market three months to 12 months.

Barry MacCarthy - Royal Bank of Scotland - Analyst

Thank you.

Hilde Nafstad - Statoil ASA - Head of IR

Do we have any more questions, operator?

Operator

Yes, ma'am, we do. One moment, please.

Michael Alsford - Citigroup - Analyst

Hi there. It's Michael Alsford from Citi. I've got two questions, please. Just, firstly, on the natural gas market in Europe, could you maybe give a bit of color as to what you're seeing currently from your gas buyers and whether you're seeing an increased offtake from your long-term contracts currently, given we're seeing, obviously, higher spot prices at the moment and the fact that maybe they see the incentive to take volumes under their long-term contracts currently because you seem to be talking down a little bit of production for second quarter and third quarter?
And, then secondly, just on the Gassled; you highlight you might potentially sell your equity stake in Gassled, could you maybe give a bit more color as to are you looking to completely divest of your stake in Gassled or are you looking to take a partial sale? And maybe a little bit on the timing as to when we might see you looking to divest of that stake. Thanks.

**Torgrim Reitan - Statoil ASA - CFO**

Okay, thanks. First, on the outlook European gas markets. It has been a market with quite a bit of turbulence over the last few years, and in my previous job I headed up trading activities within natural gas. From 2009 and onwards, we were actually surprised by two things; one was the strength of the recovery and of the demand recovery, especially in Germany; and the second one was the increased demand for gas towards Asia. That surprised us on the upside so the markets firmed up quite rapidly. And I would say, actually, both of those two points are still valid, going forward.

The prices, currently, they are quite healthy. If you look at the spot prices in a historic context, it's around 2006/07 levels, '07 levels I think, which is good. And natural gas competes, currently, very well with alternative sources of energy. We see that both the case that German nuclear capacity is down and also the tragic situation in Japan. Japan, after the tsunami and earthquake, has actually firmed this up further.

We see a European gas market where gas is attractively priced compared to alternatives and where it is robust prices as we see it. I won’t speculate in the further development but it's an okay market to operate in and if you consider our position in this, you should remember that Norwegian gas has to travel one-fifth of Algerian gas, one-tenth of Russian gas and also one-tenth -- one-eighth of Russian gas and one-tenth of Qatari gas. And we have low unit costs for our gas and we have access to all the landing points so we consider ourselves to be very well positioned for what's to come in that market.

When it comes to Gassled and sales process, you are right, we are evaluating the assets and evaluating whether that has more value for others than for us, so we are thinking about it. I will not go into any specifics on the timing of it but you are right, we are thinking about that asset.

**Michael Alsford - Citigroup - Analyst**

Okay, thank you.

**Hilde Nafstad - Statoil ASA - Head of IR**

Next question, please.

**Operator**

Yes, ma’am.

**Brendan Warn - Jefferies International - Analyst**

Right, thanks. This is Brendan Warn from Jefferies. Just one quick question, Torgrim. Just as a -- I know it’s more of an over-horizon indicator of costs than a reflection of your cost reduction, just can you make a comment on the trend of the total recordable and lost-time injury frequency? It looks to be heading or trending back up to where you were at 2006/2007.
Torgrim Reitan - Statoil ASA - CFO

Yes, on -- that was the lost-time frequency and so they have -- if you look at safety KPIs in general, it is a positive trend over the years. The serious incident frequency, which is the one that we consider the most important one, we have reduced that significantly over the years. I think it was around six in 2006; in 2010 it was 1.4 as far as I recall, and this quarter it is 1.2, so that is progressing well.

When it comes to the other ones, I’m not prepared to answer, in detail, the explanations of those developments. But I can make a general reflection on the importance of safety, which is, to our Company, extremely important and we consider ourselves to be good in that respect but we need to be better and better and better.

And I will encourage you to -- there is a letter to the PSA authorities after the Gullfaks incident, which was an important learning exercise for the Company. That was an incident where the barriers functioned but it had a potential; we agreed to that. But for us it’s important that we never, never get complacent when it comes to safety; we need to be better every day on this one. We are progressing and have full attention to it.

Brendan Warn - Jefferies International - Analyst

Thanks.

Hilde Nafstad - Statoil ASA - Head of IR

Do we have any further questions from the audio audience?

Operator

Yes, we do, ma'am. Just one moment, please.

Lucy Haskins - Barclays Capital - Analyst

Good afternoon. Lucy Haskins from Barclays Capital. Torgrim, you talked about more downside risks to the production guidance for this year and talked about gas offtake; are you also starting to see a higher incidence of unplanned maintenance on the NCS? And how much contingency are you building into your forecast for this year and indeed the 3% per annum growth rate out to 2012 by nature of perhaps the slightly aging productive capacity in that part of the world?

Torgrim Reitan - Statoil ASA - CFO

Okay. A very good question, thank you. On -- I deliberately said that that is more downside risk than upside risk in the production in 2011 compared to 2010 and I said that in February at the Capital Market Update, and it is still valid. The main risk elements related to this year is ramp-up of production from new fields. It is maintenance that we are able to deliver on the maintenance program and step up the production after the maintenance program, which is as important. It is related to gas offtake situation over the year, and it is also related to opportunities in the gas market to defer gas production to a later point in time. That is the main uncertainties.

Furthermore, we have not catered for large incidents beyond what you should expect from a company like ours. You should expect that we will have unplanned losses as we operate a significant portfolio but we’re not catering for, for instance, incident like the Kvitebjorn pipeline a few years back when someone dragged an anchor over a pipeline and destroyed it, so we are not
catering for that. Furthermore, I will remind you that we said 2010 level or slightly lower so that is the wording that we use on it. We are -- we have produced, so far, this year, as I should expect, but it's not more than what it should be.

When it comes to unplanned losses so far this year, we have had some. If you look at the rate compared to earlier year, it's approximately where it has been over the last period, as such, so no big changes in that respect.

Lucy Haskins  -  Barclays Capital  -  Analyst
Many thanks.

Hilde Nafstad  -  Statoil ASA  -  Head of IR
Next question, please.

Jon Rigby  -  UBS  -  Analyst
Hi. It's Jon Rigby from UBS. Two questions on tax and then just a follow-up on Peregrino.

On tax, can you just confirm whether the guidance you're providing on the international tax rate is a permanent feature or just one that's related to current producing conditions and oil price?

And the second, and I almost hesitate to ask this, but when you clean up your financial items and still get a charge for the year, you appear to also show a charge on -- a tax charge, i.e. a tax charge on a charge; I just wondered what was going on there and what we could expect, on a cleaned-up basis, what your tax rate would be on financial items.

On Peregrino, can you just confirm -- have you received some cash already? Is there a net cash to balance to be received or are you getting the full amount in the second quarter? Thanks.

Torgrim Reitan  -  Statoil ASA  -  CFO
Okay, thank you. Kaare, you can start preparing for the question on financial items and tax.

When it comes to international tax, I understood your question whether this was a permanent change in the tax --.

Jon Rigby  -  UBS  -  Analyst
Yes.

Torgrim Reitan  -  Statoil ASA  -  CFO
-- expected tax internationally. The tax rate in this quarter was very high in the international segment. You should also expect it to be 50% to 55% over the next year or so. We have earlier guided on 40% to 45% so, yes, in the short term, you should expect
increases increasing in the tax rate internationally. However, Peregrino is stepping up and our production in the US and Canada is stepping up with much lower tax rates so that will drag it down over a couple of years, so that is what you should expect.

And then just the reflections on other things to look out for in the international segments. When we are drilling wells, if we are drilling wells in countries where we don’t have a tax protection or a tax position, it will typically impact more on the tax rate than else, for instance, the Ñiwi well this quarter. And in earlier quarters, we have had dry wells in the Gulf of Mexico and in the US we don’t have tax protection either for accounting purposes so dry wells in those areas will typically drag up the tax rate within the international segments.

When it comes to Peregrino, yes, we have received the money to Peregrino. There was -- that was received in late April so that sits in our accounts.

Jon Rigby - UBS - Analyst
But was that the full -- that was the full amount of disposal or had you received and advance?

Torgrim Reitan - Statoil ASA - CFO
Yes, that was the full amount so that is fully paid and sits in our accounts, so that is fully received.

Kaare Thomsen - Statoil ASA - SVP for Accounting and Financial Compliance
The tax rate on financial items is a hard one to predict because it all depends. You have -- in the Group we could have currency losses in one jurisdiction and gain in another jurisdiction. And also the tax rates vary very much from approximately 20% up to 60% to 65% for the net financial items. Especially when the net financial items come down to zero, it could be any percentage, the tax rate; as it is now, it’s minus 114%. But what we say if we have to say a figure, which should be an average figure, we have said 40% to 45% on the net financial items, but that is the tax item which can vary the most in the whole composition of the tax.

Jon Rigby - UBS - Analyst
Okay, perfect. Thank you.

Hilde Nafstad - Statoil ASA - Head of IR
Right, I think we will run off one last question if there are any more questions in queue.

Operator
Very good, ma’am. We actually do have one question; I’ll put that one in right now. Please hold.

Theepan Jothilingam - Morgan Stanley - Analyst
Hi, it’s Theepan here, at Morgan Stanley; just a couple of follow-up questions. Firstly, could you -- just on volumes, could you give us an estimate of where you think year-end production would be for Peregrino; the exit rate?
And, then secondly, just if you could give us an update in terms of where we are on final investment decisions for some of the key projects for this year.

And, then lastly, I think on the Skrugard announcement you suggested the potential for an appraisal well; I know you're going to be drilling another well on the license for next year, I was just wondering when do you think that appraisal will maybe drill?

Torgrim Reitan - Statoil ASA - CFO

Okay. The year-end production on Peregrino, I will not give an estimate on that one. What I can say is that it's going to be 37 wells in that license and they will have -- each of them have a significant contribution, as well. We are progressing on preparing the wells and there is wells tied up already so the step-up is progressing as expected when it comes to Peregrino.

When it comes to key projects for this year step-up, we had touched upon Peregrino. We have Skarv as a key project for production in 2011; that is BP-operated and that is expected to start up in the second half of the year. We have Pazflor, which is a Total-operated license in Angola. That is going to have a large impact in 2012 but we expect it to start up in the very end of 2011. And then I would like to mention shale, Eagle Ford and Marcellus which are stepping up. We have rig crew and frack crew available that we need to build it up and it is building up as expected, as such. But that is, as you know, invest and drill as you go, so that might vary, going forward, on the step-up related to that. Yes, so that is the main contributors to 2011 step-up production.

Then your last question, Skrugard and appraisal well? We are enthusiastic about the area, and so on, and we have more work to do up there. I'm not prepared to discuss on when that is going to happen but it is important for us to firm up the volumes in that area so we can mature it even further.

Hilde Nafstad - Statoil ASA - Head of IR

All right? Thank you.

Theepan Jothilingam - Morgan Stanley - Analyst

Okay, great. Thanks.

Hilde Nafstad - Statoil ASA - Head of IR

Unless -- are there any further questions in the room here in Oslo. Anne, one last question.

Anne Gjoen - Handelsbanken - Analyst

Anne Gjoen, Handelsbanken. When it comes to natural gas you previously indicated that, based on contracts renegotiated, it's basically 70% that you sell oil-linked and 30% that you sell in the spot [gas] market; is that also a good indication, going forward, if you assume a relatively high offtake?

Torgrim Reitan - Statoil ASA - CFO

I think -- just a second. I think there are a couple of points I want to make in that respect. First of all, we have in 2009 when we faced a significant drop in European prices, we renegotiated the contracts; we were early out in that respect, and then we had
a grace period for three years. What we did was to put some more spot indexations into the gas formulas; together with that we had excess capacity to pipelines and liquid markets so we could operate that.

When that is said, when it comes to the mix of spot, going forward, you should expect, actually, this year to be less -- don't have the specific numbers in front of me here but you should actually expect the exposure to spot to be less this year than last year. So that is -- but what we can say is that if you look at the long-term contracts, around 70% of that volume is linked to oil and gas products as such and that is still valid. And then there is a certain amount of gas with -- outside the long-term contracts as well.

Hilde Nafstad - Statoil ASA - Head of IR

Thank you. I think that will have to conclude our Q&A session and also our program for today. Today's presentation and the Q&A session can be replayed from our website and, in a few days, transcripts will be available. Any further questions can be directed to the Investor Relations Department. Thank you all very much for participating and have a good day.