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## Conference Call Transcript

STL.OL - Q2 2011 Statoil ASA Earnings Conference Call

Event Date/Time: Jul 28, 2011 / 11:30AM GMT



Jul 28, 2011 / 11:30AM GMT, STL.OL - Q2 2011 Statoil ASA Earnings Conference Call

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## PRESENTATION

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

Good afternoon, ladies and gentlemen, and welcome to Statoil's second-quarter earnings presentation 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. 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 07.30 Central European Time, we announced the results for the second quarter of 2011. The press release regarding these 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. You can find a link to the presentation on the front page of Statoil.com.

I will ask you to kindly make a special note of the information regarding forward-looking statements, which can be found on the last page of the presentation sets.

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.

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

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**Torgrim Reitan - Statoil ASA - CFO**

Thank you, Hilde, and welcome, everyone.

Before I start discussing the quarterly earnings, let me, on behalf of Statoil, express our deep-felt sympathies to the families and loved ones of the victims of the shocking terror attacks in Norway last Friday. The extent of the tragedy is incomprehensible. The international communities' engagement has been heartwarming. And on behalf of Statoil, I would like to express our gratefulness for all the kind and thoughtful words we have received from all parts of the world. But although financial results seem insignificant in this situation, our government has expressed a wish for the society to keep up normal activities to the extent possible.

As a consequence of the tragic events, questions have been asked and discussions will take place with regards to the security and safety of our installations. The oil industry has procedures in place and routines for monitoring threat levels. The Norwegian authorities and police evaluate and advise on changes in threat levels. We will follow guidance and instructions given by Norwegian authorities, and there are no indications at this time that there will be a permanent change in threat level.

I will now present our earnings for the second quarter of 2011, a quarter with very strong financial results. In fact, the net income this quarter is all-time high in Statoil's history. So, let's turn to the highlights of the last three months.

First of all, we have had excellent exploration results this quarter. The activity in the quarter has been high and in line with our sharpened exploration strategy, with more high-impact wells and strengthened access to acreage. We completed a total of nine exploration wells and announced six discoveries in the period. Amongst these were two high-impact discoveries, the Skrugard discovery in the Barents and Peregrino South in Brazil.

We also accessed new acreage, offshore Canada and in Indonesia, in addition to the 21st licensing round in Norway. Drilling resumed in Gulf of Mexico, where we, as an operator, are currently drilling the Logan well, one of our nine high-impact wells this year. And drilling has also started in the partner-operated Kakuna well, operated by Nexen. We will continue with our high exploration activity also in the quarters to come.

We have seen strong commodity prices in the quarter, and the oil prices have been at the second-highest level the quarter that has passed. And we have again delivered a very strong cash flow, NOK120b in cash flow from underlying operations so far this year, and this has strengthened our balance sheet further. Our net debt to capital employed is now at 14%. That is down from 25% at year-end. And in a situation with significant uncertainty regarding the macro development, I find it prudent to run with a solid balance sheet.

The operational performance has been in line with what we expected, and production has been impacted by extensive maintenance and also by seasonal low gas off-take. And this is in line with what we discussed at our first-quarter presentation and our Capital Markets Day in June.

We have made good progress in maturing our project portfolio, underpinning production growth all the way to 2020, as laid out in New York in June. In the second quarter, three projects have received approval from the government, of which two were fast-track projects.

But let me express my deep-felt sympathy with the Ministry of Petroleum and Energy. The tragic terror attacks last Friday targeted the government and the ministries, including the MPE. And we are impressed by the Ministry that the Ministry is able to keep up their activity even under these circumstances, with their offices being destroyed. Our thoughts are with them in these difficult times.

I would like to point out one of the fast-track developments, the Hyme project in the Norwegian Sea, where we submitted the development plan on May 12. And we received the approval of the development plan only one and a half month later, and I would like to compliment the authorities for the swift delivery. I see this as a proof that fast-track developments are considered an important measure for further development of the established petroleum provinces.

There are five more fast-track projects in the pipeline to be submitted for approval later this year. So, all in all, nine fast-track projects this year. And the first nine, they will give production of more than 70,000 barrels per day in 2014, at a breakeven of around \$40 per barrel.

We have recently announced that we have awarded contracts for category D rigs, a rig designed by Statoil, especially tailored for the NCS production drilling, underlying our efforts to take out the maximum value from the NCS.

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And we continue to create value through portfolio optimizations. And this quarter we closed the Peregrino transaction, generating a gain pre-tax of NOK8.8b and NOK7.5b after tax. And we continue to sharpen Statoil as a technology-focused upstream company and have agreed, as you know, to divest the majority of our Gassled operatorship -- ownership. And we expect to close the transaction by end of 2011. However, this is pending authorities' approval.

Then, over to production. Equity production in second quarter was 1.692m barrels per day. This was 14% lower than the second quarter last year, and this is in line with our expectations. The production is okay, and it is consistent with our guidance. The production was affected by an extensive planned maintenance program, taking out around 100,000 barrels per day in the quarter. 70% of this was related to liquids.

Productions from new fields like Peregrino and Leismer is ramping up, and this is starting to contribute. We expect to see other fields, like the Pazflor field in Angola, to start production in the early part of the fourth quarter. The Skarv field will, according to the operator, now start production in the fourth quarter 2011. And as I said in New York, the delay will impact us by around 10,000 barrels per day in production in 2011.

Snohvit is back in full production after a delayed startup after the turnaround. Snohvit produces at very high production rates when in production mode but, as you know, we have had to replace part of the equipment over the last years.

In addition, we have had some unplanned outages related to risers on Njord, Visund and Snorre B. Njord was shut down after findings on one of the risers, as part of a planned inspection. As a precautionary measure, several of the risers on Visund and Snorre B were also closed for further assessment. Part of the production have resumed at Snorre B and Njord, and we are in process of replacing the damaged risers.

Internationally, there were decline in fields in Angola and Gulf of Mexico, and some operational issues in Angola and Azerbaijan. As is normal for this time of year, we are experiencing seasonal variations in the gas off-take. You may recall that in second quarter 2010 we sold significant volumes in the spot market. This has not been the case in the second quarter 2011, and this is due to the reduced production permits on Ormen Lange and Troll.

I can also mention that we have now been granted a full production permit for the Troll field, for the gas year starting October 1, 2011. And this will give us higher production and higher flexibility in optimizing our gas position. As always, we are evaluating to defer gas production into future periods if the forward curve yields a higher return than producing and selling the gas now. Currently, the curve give incentives to defer gas production, and this is likely to happen in the second half of the year.

We are also continuing to see the effects of the Gullfaks well integrity shut-in, which has temporarily taken out approximately 30,000 barrels per day. Gullfaks develops as expected, and we have not encountered negative findings. We have started production from some of the wells, and we will gradually increase production from the field.

We have also started production from Beta West in the Sleipner area. This is a discovery which we did back in 2009, and it is now already in production. Compared with last year, we have also higher production from new fields like Morvin and Vega, and we are also ramping up production at Tyrhans.

Net operating income was NOK61b, an increase of NOK34b over the same quarter last year. This results in a net income of NOK27.1b, and this is the highest in Statoil's history. This was largely driven by high commodity prices in the quarter, and in addition Statoil booked a gain from the Peregrino divestment during the second quarter. Increased prices for liquids and gas impacted our results positively by NOK16b. And production was, as mentioned, lower this quarter, and the reduced lifting of oil and gas impacted the results with NOK7b, negatively.

As always, we make adjustments to be able to characterize the underlying earnings, and this quarter the adjustments add up to NOK17.4b. This is a very high number, and it relates to the booking of the gain on the Peregrino of almost NOK9b, from a reversal of previously impaired exploration expenses of NOK2.2b, from changes in fair value of derivatives in the MPR division contributing positively with NOK3.7b, and from effect of realized and unrealized gain on commercial storage NOK2.5b, and the lift position NOK2.2b.

As a result, the adjusted earnings before tax was NOK43.6b, compared to NOK36.5b in the same period last year. This is a 20% increase, compared to the same period last year.

Adjusted exploration expenses decreased by NOK1.4b, compared to the same period last year, and this is mainly because of successful drilling results leading to a higher proportion of expenditures being capitalized.

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I will revert to the tax rate in a minute, but the reported tax rate was 56% in the quarter. Based on adjusted earnings, it was close to 71%. Therefore, the adjusted earnings after tax increased to NOK12.8b, compared to NOK10.6b the same period last year, and this is an increase of more than 20%.

Then over to the business areas, a few comments on those. Development and Production Norway delivered adjusted earnings before tax of NOK37b, and this is an increase of 27% compared to the same quarter in 2010. Increased liquid and gas transfer price impacted the results by NOK13.2b, and the 7% lower lifting partly offset this and impacted earnings with NOK5.4b.

The cost development on the NCS is healthy, and our operating expenses and SG&A are in line with last year's numbers, despite more fields have been put into production. The focus on cost-efficient operations will continue.

Then over to the international business. International Development and Production delivered adjusted earnings before tax of NOK5.8b, and this is an increase of 100% compared to last year. Increased prices impacted the results by NOK2.8b, and this was partly offset by 11% lower entitlement production due to shut-in production in Libya and decline in fields in Angola and Gulf of Mexico, and some operational issues in Angola and Azerbaijan. Exploration expenses were NOK900m lower this quarter, and this is due to a high success rate leading to a larger portion of costs being capitalized.

The business area Marketing, Processing and Renewable Energy delivered an adjusted earnings of NOK500m this quarter, and this is NOK2.9b lower than second quarter in 2010.

For natural gas, the main contributors to the lower results were reduced gas sales in the quarter. We also realized losses on financial positions related to time optimization of gas production. However, this strategy, which implies moving gas volumes between time periods, is still profitable for Statoil on an overall basis. But as you know, the results from moving gas in time will mainly be shown in the Development and Production Norway's results, through higher volumes at a point in time, with higher prices. And lastly, decreased income from Gassled caused by decreased ownership share and lower tariffs.

For crude oil processing, marketing and trading, we experienced weak trading results. The quarter has been challenging and characterized by backwardation and a lower quarter-end price than opening price. We have in the past had significant positive contributions from our trading activities in both crude products and natural gas. And the nature of this business is that it is volatile from quarter to quarter, and we should expect that, but it contributes, on average, very positively.

Refining margins were, as you know, unusually low for the season.

The tax rate on the reported results was 56%, and 71% on the adjusted earnings. The gain on Peregrino transaction has a low tax rate, and this combined with the reversal of previously impaired explorations in areas without tax protection resulted in a lower than normal tax rate in our International segment. These are the main explanations for the difference between tax on the reported results and adjusted earnings.

The adjusted tax on our international upstream business was 49% this quarter. We have previously guided on a tax rate, internationally, of 50% to 55% in the short term, and I expect this to trend back to 40% to 45% in a few years. So you should, as such, expect a somewhat higher tax rate within the International segment for the next quarters.

Within the MPR segment, the tax rate is a consequence of the earnings composition, and I expect the combined MPR tax rate to be around 70%. But you should expect the tax rate within this segment to be volatile, based on the composition of the earnings. This will be especially visible after we have closed the divestment of the majority of our Gassled position.

On a corporate level, the adjusted tax rate was close to 71%. I said earlier this year that you should expect the rate to be in the upper range of our guiding, 70% to 72%, and this is still valid.

Cash flow from underlying operations in the first half of the year was NOK120b, and the strong cash generations was driven by the high oil and gas prices, as well as proceeds from sale of assets. These transactions have generated substantial value for our Company.

Our balance sheet continues to strengthen, and net debt to capital employed is now 14%, as I said, by end of the second quarter. And I expect it to decrease further, and estimate it to be around 10% by the end of the year. Proceeds from the Gassled divestment will reduce it further.

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As I said at our June event, financial flexibility is very important. An appropriate capital structure is balancing capital distribution, financial targets and securing sufficient financial flexibility, and I'm comfortable with the current financial strength.

In the first half, we paid NOK45b in taxes and had net investments of NOK9b. In the third quarter we will have one tax payment, and we will have two in the fourth quarter. Tax payments will be higher in the second half of the year than in the first half of the year, due to higher commodity prices.

NOK20b in dividend for 2010 was distributed to shareholders on June 1, and this represents an increase of 4.2% since last year and a direct yield above 4%.

At our Capital Markets Day on June 20, we communicated an updated outlook, all the way to 2020. I will now quickly discuss the short-term outlook.

We expect 2011 CapEx at approximately \$16b and exploration activity of approximately \$3b this year. We expect our production to grow at approximately 3%, on average, for the period 2010 to 2012. And as I said at the start of my presentation, our second-quarter production was in line with our expectations.

As we discussed in New York, the operator has announced the delayed startup of the Skarv field to late 2011. And the current market situation implies favorable conditions for deferral of gas sales, which will be in accordance with our value-over-volume strategy.

Major new fields will come on-stream this year and contribute to the production. Peregrino, Pazflor and Skarv will add to the production towards the end of the year. So, we expect equity production in 2011 to be slightly below the 2010 level.

Like I said in the first-quarter presentation, the combined production from NCS for second and third quarter will be in line with last year, but more evenly distributed. In the third quarter, we will still see extensive maintenance effects, estimated at 70,000 barrels per day on NCS and internationally. Around 80% of this will be related to liquids. In sum, I expect total maintenance to have an impact of 50,000 barrels per day over the year, and this will mainly be related to liquids production.

So, this concludes my presentation, so thank you for your attention. And I will then leave the floor to Hilde again, to help us through the Q&A session.

## QUESTION AND ANSWER

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

Thank you very much, Torgrim, and we will now turn to the Q&A session. And for this session, Torgrim will be joined by Senior Vice President for Accounting and Financial Compliance, Kare Thomsen, and the Senior Vice President for Performance Management and Analysis, Svein Skeie. This session will last for approximately 15 minutes. I will ask you to please limit yourself to one question at a time. Operator, do we have any questions in queue?

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**Operator**

We will currently take our first question. [Jonathan Amorel] from Goldman Sachs, please go ahead. Jonathan Amorel from Goldman Sachs, your line is open.

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**Jonathan Amorel - Goldman Sachs - Analyst**

Sorry. That was a mistake.

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**Operator**

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Mr. Amorel, your line is open. Would you like to ask a question? We will now take our next question. Barry MacCarthy from Royal Bank of Scotland, please go ahead.

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**Barry MacCarthy - RBS - Analyst**

Good afternoon, Torgrim. Thank you for the presentation. Just to go back to cash flow, you gave some indications in New York about perhaps achieving cash flows of about \$20b as an indication for the year, assuming Brent at \$107 a barrel from that point. You seem to be operating on a run rate quite considerably better than that, and I wondered if you thought that the \$20b number would probably be higher rather than lower over the balance of the year, and giving you that extra balance sheet flexibility that you rightly think is important.

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**Torgrim Reitan - Statoil ASA - CFO**

Thank you. The cash flow from operations is, of course, dependent on oil and gas prices as such, so we are building a strengthened balance sheet. But what we see is very much in line with what we have said also in New York. We expect net debt to be around 10% at year-end, given the current market, and there has been no change to that. So things are as they were in New York. There are of course substantial upside if prices are high and higher than they are today.

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**Barry MacCarthy - RBS - Analyst**

Thank you.

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

Next question, please, operator. Operator, do we have another question?

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**Operator**

Michael Alsford from Citigroup, your line is open.

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**Michael Alsford - Citigroup - Analyst**

Good afternoon. A question actually still on the balance sheet, actually, and around your net debt target of 10% for the end of the year. If you look at, I guess, historically, it's significantly lower than what your gearing's been in the past. Could you maybe give a bit of color as to why you think you need to be so conservative on the gearing target and perhaps talk a little bit more about why that kind of target is in place, and if there's any room to potentially increase dividends or is there going to be a change in dividend policy as a result of that gearing target being at that kind of level? Thanks.

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**Torgrim Reitan - Statoil ASA - CFO**

All right. Thank you. So this is more like a forecast on how we see the balance sheet develops towards the year-end. So I find it prudent to run with a solid balance sheet, given the uncertainty that we are facing. We are compared to peers. Our peers seem to have a solid balance sheet, as we go. And I think it reflects the same sort of thinking that we have in-house, that there is -- we are in a long lead time business. We need to have a solid balance sheet, given the uncertainty that we face in the macro.

And there are also some learnings from the Macondo incident, that companies that are running operations like ours are risky. And the importance of having a solid balance sheet and significant liquidity available at all times is very important. So that is reflecting our thinking as well.

We have currently a credit rating of AA-. It is of course comfortable, as such. So it is a comfortable situation, given all the things that we see.

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When it comes to the dividend policy, we have a policy that states that we are going to grow our cash dividend in line with long-term underlying earnings, as such. And if you look at the history of our dividend, our capital distribution, it has been quite good and around 50% payback. We also had that for 2010, and that gave a direct yield of above 4% at that point in time. So the dividend policy remains firm. The balance sheet is solid, so it will be solid enough to honor the dividend policy going forward.

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**Michael Alford - Citigroup - Analyst**

Okay. Thank you very much.

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

Next question, please, operator.

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**Operator**

Our next question is from Teodor Nilsen from First Securities. Please go ahead.

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**Teodor Nilsen - First Securities - Analyst**

Yes. Hello. I have a question regarding the production cost of the Norwegian operations. This quarter or the second quarter reported an OpEx per barrel of \$9.7, and that's a record high. And it's significantly up from \$7.4 in the first quarter. So I just wondered, could you please give some colors on why the OpEx is that much up -- more up than the general energy prices are up?

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**Torgrim Reitan - Statoil ASA - CFO**

Okay. I'll leave the word to Svein Skeie.

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**Svein Skeie - Statoil ASA - SVP, Performance Management & Analysis**

Yes. Thank you. As you said, our production cost on -- in the Group is somewhat up. The main reason for increased production cost is then reduced production. If we look at the Norwegian continental shelf, if you look at absolute level of the cost, it is only a slight increase compared what we've seen last year. That is partly due to the fact that we have had some new fields which are ramping up. But that has mainly been offset by high cost focus on the producing fields. And we are focused on the efficiency of the Norwegian continental shelf. It's very high on our agenda. And we will then have an ambition also, going forward, to stay in the top tier with our unit production cost.

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**Teodor Nilsen - First Securities - Analyst**

Okay. I also have a question on the gas prices, if I may. The gas prices realized for the second quarter was maybe slightly on the soft side. Is that a result of a higher portion from the US on low prices, or is it just because the realized prices on the European volumes have been lower than expected?

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**Torgrim Reitan - Statoil ASA - CFO**

Yes. Gas prices in the second quarter was NOK2.06 realized prices. So, in a historical context, that is a very good price for gas in Europe; let me say that first. However, the price is impacted by the trading activities in the quarter, some losses on financial instruments that goes into that realized price. So that is impacting the reported price. So you are right, without that, the price would have been somewhat higher.

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**Teodor Nilsen - First Securities - Analyst**

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Okay. Thank you very much.

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

Can we have the next question, please?

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**Operator**

Our next question is from Brendan Warn from Jefferies. Please go ahead.

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**Brendan Warn - Jefferies - Analyst**

Thank you. Just one question, just on Dalia in Angola. It just looks like production's down this quarter. Are we expecting that going forward? And just what's the reason behind it, please?

Actually, if I can have one other quick short question, just on your Snohvit and uptime expectations for 2012. Are we through the worst with Snohvit or what are we to expect going forward?

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**Torgrim Reitan - Statoil ASA - CFO**

Okay. Thank you. I'll take the Snohvit question and then, Svein, you can answer the Dalia question.

So Snohvit is currently at full production and it produces very well. As you know, we have changed some part on Snohvit that has not been working, and that was done successfully this summer. So now it's back. So there are some planned maintenance stops going forward, not this year but later. So based on what we think, this is now fine for producing all the way to the next maintenance stop.

When that is said, Snohvit is a largely complex field and it is a one-line production facility. So either it produces or it is not producing, as such. So when operational things happens, it has typically a large effect on the production. But Snohvit is functioning well. I will never give guarantees, as you know. But as we see it, it -- we don't have to do more until the next planned maintenance stop on Snohvit.

Okay. And then on Dalia, Svein.

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**Svein Skeie - Statoil ASA - SVP, Performance Management & Analysis**

Yes. On Dalia, as you commented, there has been lower production in Dalia this quarter compared with the last quarter, last year. The main reason for that one is that we have had some extended turnarounds for Dalia in the second quarter of this year, compared to what we had with the production that we had last year.

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**Brendan Warn - Jefferies - Analyst**

Okay. Thanks.

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

Do we have any further questions, operator?

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**Operator**

You currently have four more questions. We will take our next question from Oswald Clint from Sanford Bernstein. Please go ahead, sir.

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**Oswald Clint - Sanford Bernstein - Analyst**

Yes. Hi. Good afternoon. Could I just confirm the Troll production permit you have for the next gas year, rolling into 2012? Was -- that was included in next year's overall production guidance, is that correct?

And then, secondly, I was just curious if there was anything you could update us on progress with West Qurna-2. Thank you.

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**Torgrim Reitan - Statoil ASA - CFO**

I didn't get your last question, so -- but let me answer your Troll question first, and if you can repeat your last question afterwards, that will be appreciated.

When it comes to Troll production permits, we -- the reduction that we had for the gas year we are in, we consider that to be of a temporary character and expected that to come back. And that happened, so we had that in writing during the summer. So from October 1 it will produce -- we will have the full production permit back on Troll. This is something that we have expected and this is something that we have based our outlook for over the last year. So this will not change what we said at the first quarter and at the Capital Markets Day in New York in June.

If you could repeat your second part of the question, that would be good.

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**Oswald Clint - Sanford Bernstein - Analyst**

Yes. It was referring to down in Iraq and predevelopment, early drilling at West Qurna-2 field, given that it was expected or is expected to maybe see some volumes at the end of next year, going into 2013.

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**Torgrim Reitan - Statoil ASA - CFO**

Yes. First of all, LUKoil is the operator in West Qurna-2, so they will need to give specific guidance on the startup and so on. But in general terms, this is one of the world's largest undeveloped fields. LUKoil is the operator. We are -- have seconded personnel into that organization. We have received a preliminary development plan; I think that was approved in November last year or late last year. So this is underway, as we see it. But I think the right company to ask for specific guidance on that will be LUKoil, actually.

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**Oswald Clint - Sanford Bernstein - Analyst**

Okay. That's good. Thank you.

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

Next question, please.

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**Operator**

Our next question will come from Nitin Sharma from JPMorgan. Please go ahead.

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**Nitin Sharma - JPMorgan - Analyst**

Hi. Thanks. Two questions, please. The first one, and clarify if I heard it wrong, H1 on H1 the volumes have declined 12%. And what I heard you say was that in quarter three and quarter four we should expect volumes to be largely flat. And on top of that, the guidance seems to be that we should expect slight decline in '11 versus '10. How does that all stack up? And maybe I've missed something. That was the first part of my question.

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The second part was you also mentioned that you're likely to move gas volumes forward. Now, does this have any implication for your '10/'12 production growth guidance? Thank you.

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**Torgrim Reitan - Statoil ASA - CFO**

I think that was more or less the same question, one question, as such. So, yes, we expect 2011 production to be slightly below the 2010, so this is what we have discussed in New York and so on. It is linked to moving of gas in time. Currently, we have -- in the portfolio we have flexible gas fields, like Oseberg and Troll, where we have flexibility to produce when the prices are highest. And currently, the market and the curves give incentives to produce, to move some production from the second half of the year into future periods. So that is likely to happen.

So we are -- so that is what is new since we discussed this last time. So we expect it to be slightly below 2010. And this is very much in line with our value-over-volume strategy within the gas business.

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**Nitin Sharma - JPMorgan - Analyst**

Thank you.

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

Right. We'll take the next question.

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**Operator**

Our next question is from Jon Rigby from UBS. Please go ahead.

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**Jon Rigby - UBS - Analyst**

Yes. Thank you. I think it's always the way when you change disclosure that suddenly numbers start changing from their long-term trends. So I just wanted to just deepen into the gas trading disclosures, if I could. You mentioned that it was related to I think what you've just mentioned about selling gas forward or leaving gas to sell forward. Can you just talk around that a little bit more and how that actually affects the interaction between your NCS or your upstream businesses and this gas trading business, because is it just the absence of profitability or is there actual economic profit moving between the two divisions, please? Thank you.

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**Torgrim Reitan - Statoil ASA - CFO**

Okay. Thank you. In my previous job, I headed up trading activities and short-term activities and optimization activities in gas, so I hope I can explain it in an understandable way. So it is back to these two flexible gas fields that we have, Oseberg and Troll, where we have the opportunity to turn up and down the production and so on. And, of course, the asset sits in the DPN business area, while the trading activity sits in the natural gas area, as such.

So let me use an example, that we take 1bcm of gas and move from summer 2011 to summer 2012. So the way it will show up in the results of DPN is only in a way with lower gas production in 2011, and then with a higher gas production in 2012 at a higher price, as such. So there's a lower EBIT in one year and then an even higher EBIT the year after.

So the way it works in the accounts of natural gas or MPR is that they trade around this. They elect whether they want to lock in the spread between the summers or whether they want to leave the spread open. And they can go -- they can use that for trading purposes. And then you'll have gains or losses on those derivatives that you buy or sell. So it is the derivative gains or losses that will show up in the natural gas business, and then it is the EBIT effect from the production and the prices -- realized prices that will show up in the DPN's accounts.

I'm not sure if you fully understood it, but that is the way it works. So this quarter the natural gas business is impacted by derivative losses related to this strategy, as such.

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**Jon Rigby - UBS - Analyst**

So you're saying it's basically the mark-to-mark differential between summer prices this year and summer prices next year that affected the quarter. Would that be the way of looking at it, in MPR?

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**Torgrim Reitan - Statoil ASA - CFO**

That will be part of the natural gas results. This quarter, I think it is more related to a realization of a sale that had carried mark-to-market exposure.

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**Jon Rigby - UBS - Analyst**

Okay. All right. Thank you.

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

Okay. We will take one last question, please.

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**Operator**

Our last question comes from Kim Fustier from Credit Suisse. Please go ahead.

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**Kim Fustier - Credit Suisse - Analyst**

Yes. Hi. Good afternoon, gentlemen. I actually have two questions, if I could. Firstly, just on your UK North Sea projects, you've restarted studies on Mariner and Bressay. Could you just comment on the economics of these projects, given the UK North Sea tax changes? And how do they stack up against other projects in your portfolio?

And my second question is just regarding this article we saw in the trade press, stating that Statoil has a backlog of about 500,000 man hours on the NCS, based on a recent audit of your platforms by the Petroleum Safety Authority. Could you maybe comment on this? And how do you intend to address this criticism? Thank you.

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**Torgrim Reitan - Statoil ASA - CFO**

All right. Thank you. Two very good questions. So it's good to end with good questions, and I think all questions have been good, so I'm not insulting anyone. I'm sorry about that. But Mariner and Bressay first.

Yes, as you know, quite a noisy process related to this. And I guess Mr. -- the Finance Minister in the UK surprised us quite a bit with the change in the tax rate. We have had extensive discussions with the UK government over the last months. And now they have changed the tax rules related to uplift, as such. So that is compensating for the profitability loss we had on Mariner. And Mariner is an important project for Statoil and it's an important project for the UK.

So now we're back with the same profitability, same breakeven price as we had before the change came. So that is very much appreciated. And I will -- we have appreciated working together with the UK authorities in this respect. So we are moving forward with Mariner and planning for that full speed ahead.

When it comes to what sort of impact that will have on other type of fields, is that, yes, it will have positive impact on new developments as it provides a higher uplift. So, we net the tax changes, we'll be taxing higher existing production and giving incentives to investing in new production; not a bad solution.

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Then, on the letter from Norwegian authorities on the maintenance, as such. We have -- and the safety issue. We have received a letter and we're going to reply in September related to that. I think if you look at the statistics first on serious incident frequency, we have reduced that from 6 in 2006 to 1.4 in 2010 and 0.9 now in the second quarter of 2010. So the statistics is going in the right way.

If you look at what we call outstanding maintenance hour on technical critical equipment, that has been reduced from 37,000 hours down to 13,000 hours over the last year. So we are working extensively to keep or set our fields up to shipshape, and it is in good shape. But we will always need to be better when it comes to the safety work. We can never relax. We always need to improve. So we are working together with the authorities on this issue and will address it with them in September.

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

Thank you very much. That will 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 at Statoil.com. Any further questions can be directed to the Investor Relations department, as usual.

Thank you all very much for participating and have a good day.

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