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STL.OL - Q2 2016 Statoil ASA Earnings Call

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OVERVIEW:

Co. reported 2Q16 IFRS net operating income of $180m.

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PRESENTATION

Peter Hutton - ***Statoil ASA - IR***

Ladies and gentlemen, welcome to the Statoil 2Q 2016 conference call. The format for the call will be that Statoil CFO, Hans Jakob Hegge, will run through the results and key drivers. And then we will open for questions and answers. I'm also joined by Svein Skeie, Head of Performance Management and Risk; and Orjan Kvelvane, Head of Accounting.

We aim for the call to run for around an hour today and expect to be able to cover all your questions in this time. The operator will explain the procedure again after the presentation in a second.

And with this, I turn the floor over to Hans Jakob to run through the results.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Peter, and welcome to everyone to this second-quarter analyst conference. Statoil presented adjusted earnings before tax of $913 million for the second quarter of 2016.

The second quarter was characterized by the following. First, the result this quarter continued to be impacted by the volatile oil prices, as well as weak NGL prices in North America and the low European gas prices compared to a year ago.

The fundamental market conditions are unchanged, but we do see signs that we may be heading towards a more balanced supply/demand picture for oil. Despite this, we must expect to see volatility for some time.

In the short term we expect continued pressure on European natural gas prices. Second, we keep on delivering strong operational performance. Our high production regularity continues, especially from our Norwegian fields, and we are ramping up production from new fields. This contributed to a production growth of 5%.

And third, we see continued gains from our improvement efforts. Adjusted OpEx and SG&A for the Group were 18% lower compared to the same quarter last year, and we are lowering our guidance for CapEx in 2016 from $13 billion to around $12 billion, reflecting further improvements in efficiency and prioritization.

We are also lowering our guidance for the exploration spending by 10%, recognizing the efficiencies, especially in drilling and wells, but at the same time capturing opportunities to increase activities in certain areas and to benefit from improved costs.

And finally, the Board of Directors has approved a second-quarter dividend of $0.2201 per share, and there will be a scrip option with a 5% discount for the second quarter.

The first scrip dividend offering yielded a 43% take-up by the shareholders, resulting in $290 million improved cash flow in the quarter.

We report an IFRS net operating income in the quarter of $180 million. This is before adjustments of $733 million, mainly related to an impairment of our Gulf of Mexico asset and the mark-to-market valuation effect of derivatives in the MMP segment.

Adjusted earnings before tax was $913 million compared to $2.9 billion in the second quarter 2015. The liquids prices that we realized was 28% lower and natural gas prices in Europe were 32% lower compared to the same period last year.

The adjusted result after tax was a loss of $28 million, reflecting a tax rate just above 100%. The high tax rate was a result of the earnings composition.

I will now move from the Group results to comment on the various segments. Development and production Norway had a second-quarter pre-tax result of $1.2 billion compared to $2.3 billion in the same quarter last year. The lower result was a consequence of the low liquids and gas prices in the quarter. Realized liquids prices fell 27% compared to the same quarter last year and the gas transfer price dropped by 42%.

The gas transfer price is a function of the various price indices, and this quarter there was a sharp drop in the season-ahead price compared to first-quarter prices.

Production grew 5% in the quarter. This, together with cost reductions and further efficiency gains, partly offset the effect of the lower prices. Natural decline was more than offset by the ramp-up of new fields, including Valemon, Goliat, Edvard Grieg, and an increase in Statoil production from Ormen Lange after the make-up period post redetermination.

As we noted after the first-quarter results, this quarter was impacted by higher costs from plant maintenance compared to first quarter 2016 and second quarter 2015. Nonetheless, adjusted OpEx and SG&A expenses year on year were reduced by 11% per barrel, and the adjusted DD&A was reduced by 10% per barrel, measured in the underlying currency, NOK. You should expect seasonal cost also in the third quarter, reflecting increased planned maintenance activity.

Development and production international had an adjusted pre-tax loss of $506 million compared to a loss of $16 million in the same quarter last year. Realized liquid prices were 30% lower than in 2015, and this was partly offset by higher production, up 4% adjusted for divestments. And we continue to see significant improvements in our cost base, with OpEx SG&A costs down 23% per barrel.

This was a result of effects of cost and efficiency measures lower diluent expenses and royalties, partly offset by costs associated with new fields on stream and higher transportation costs. DD&A increased 1% per barrel due to new fields on stream and ramp-ups.

The MMP adjusted result was $329 million compared with a very good result in the same quarter 2015 of $679 million. The lower result was largely due to lower refinery margins and availability due to plant maintenance at Kalundborg and Tjeldbergodden. Mongstad will have a planned maintenance stop during the third quarter this year.

Equity production was 1,959,000 barrels in the second quarter. This was an increase of 5% compared to same period last year. Underlying organic increase was 6%. The growth was largely a result of higher gas production from fields with associated gas, high production regularity, as well as resumption of equity volumes on Ormen Lange following the redetermination make-up period.

In addition we see ramp up of production from new and existing fields, including Valemon and Goliat on the NCS, Corrib in Ireland, as well as Julia and Heidelberg in the Gulf of Mexico. Divestment of Shah Deniz and reduced ownership in Gudrun as well as expected decline in mature fields offset part of the increase.

Cash flow from operations pre-tax was $6.4 billion for the first six months of this year compared to $11.2 billion in the same period last year. We paid two tax instalments of NOK6 billion each on the Norwegian Continental Shelf in the second quarter. From the second half we will pay taxes based on 2016 results. The instalments for the next three payments will each be NOK5 billion based on expected lower prices for 2016.

Dividend paid reflects the dividend for third quarter 2015, which was paid fully in cash, and the cash part of the fourth-quarter dividend. With cash investments of $6.1 billion for the first six months, this results in a negative cash flow of $3.2 billion.

Net debt to capital employed ended at 31.2%, impacted by a negative cash flow, offsetting for dividend and currency.

A few comments on guiding before I leave the word to Peter to lead us through the Q&A session. We maintain the production guiding and we expect an organic production growth of 1% from 2014 to 2017. We reduced organic CapEx guiding for 2016 from $13 billion to around $12 billion, mainly due to the impact of the efficiency efforts and our continued strict prioritization.

We estimate the exploration spend to be around $1.8 billion, down from $2 billion previously guided. The reduction is the result of efficiency as we plan to drill the same amount of wells as originally planned.

Thank you and over to you Peter.

QUESTION AND ANSWER

Peter Hutton - ***Statoil ASA***

Thanks, Hans Jakob. And with that we'll open for Q&A and we have some questions on the line already. And I pass over through to the Operator to run you through those procedures again. Thank you.

Operator

(Operator Instructions). Haythem Rashed, Morgan Stanley.

Haythem Rashed - ***Morgan Stanley - Analyst***

Thank you. Good afternoon, gentlemen. Thanks for the presentation. Hans Jakob, if I could just briefly cover two topics. Firstly, it seems for the quarter price realizations were somewhat of an issue, particularly when you look at the gas side in Europe and then on the -- in the internationals business, the liquid side. I just wonder if you could talk a little bit about how transitory you felt that that was or whether there is some -- a change in the Statoil business that means that some of this might linger for a period of time going forward.

The second question is really regarding your CapEx and the $13 billion going to $12 billion, clearly demonstrating the flexibility you have in moving CapEx lower with the efforts you're putting in. I just wanted to get a sense of, firstly, scope for that coming down further this year, because we obviously had last year where you brought it down on more than one occasion, and whether you felt that that was possible from what you are seeing at the moment in some of the operations and the efforts that are going on to increase efficiency.

But also just from a longer-term perspective, you highlight today that the CapEx is lower but production guidance is unchanged. Is there anything you can say about what you think medium term for Statoil the right level of CapEx is? Do you think $12 billion is a number that you can continue to spend that continues to allow you to grow at a reasonable rate and deliver on future projects? Or, at some point does that number need to go back up again to a more sustainable level? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Haythem. First on the gas price and realized prices, as you know, this is the way we sell our gas. If you look at the gas, the price markers used in the internal price is reflecting Statoil's average sales structure over a period of time. That includes a mix of short- and longer-term indices. So the main reason for the internal price decline was a sharp drop of the season ahead compared to the day ahead. Still the realized price in the second quarter was 10% higher than NBP. So in the first quarter we benefited even more of this. And then to CapEx. The CapEx rate and the guiding has been taken down to $12 billion. We maintain the strong capital discipline with strict prioritization. We see efficiencies across all the portfolio. We see it in exploration. We see it in the projects, on the US onshore. There's a downward trend across the portfolio.

We have slightly less capitalized exploration with a year-to-date capitalization rate of 31%, lowering the total spend. And the project portfolio is continuously being evaluated in this respect.

When it comes to medium-term CapEx level, I think we highlight the fact that we will have capital discipline. We will invest when the projects are clear. We have the $4 billion to $6 billion in flexibility in 2018 and 2019 and that is of high value to us. So maintaining the flexibility going forward will be important.

Haythem Rashed - ***Morgan Stanley - Analyst***

Okay. Thank you.

Operator

Mehdi Ennebati, Societe Generale.

Mehdi Ennebati - ***Societe Generale - Analyst***

Hi, good afternoon, all, and thanks for taking my question. Two questions, please, very quickly. First, I would like to come back, Hans, on what you said regarding the tax payment. So you've paid roughly $2.3 billion tax in H1 2016, mainly related to 2015. I wanted to know if or can you please confirm that we should consider a material decrease in H2 2016 tax payment given it will be related to full year 2016 earnings which are much lower than last year. If I understood well, you said that the payment should be around NOK5 billion in Q3. I just would like to know if you can confirm this. Maybe the line was not that good.

And second question regarding to the working capital. So your working capital increased materially in H1 2016, roughly $700 million. And I wanted to know what should we expect in H2 2016, some reversal or, let's say at least a kind of stabilized working capital which will not negatively impact your free cash flow? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Okay, thank you Mehdi. On the tax payment, it is a high tax rate, actually the first time above 100%. We say that the tax rate is negatively impacted by the loss in the international business in areas with limited tax protection. And going forward we will benefit from this when we start earning money, for instance in the US where we do not pay taxes.

We have a low tax rate on the adjusted earnings from DPN. That is mainly due to the higher effect of the uplift deduction due to the low adjusted earnings. We see a high tax rate on the adjusted earnings in the MMP segment. That is caused by earnings composition. And in terms of guiding going forward, in general, lower prices increase the tax rate. Over time a falling tax rate should be expected when prices recover and $700 million lower than paid in the first half if we take the actual average. So that was on tax.

When it comes to working capital, I leave the question to Orjan Kvelvane.

Orjan Kvelvane - ***Statoil ASA - Head of Accounting***

Yes. Okay. Thank you. I'm not sure if I followed your numbers, but from a working capital perspective we have a significant reduction compared to the end of same period last year, and that is of course due to prices. When it comes to the working capital compared to first quarter, we see that it's the inventory that increases and that is due to higher volumes in transit, which increases that part of the working capital. So over the past four quarters we have a pretty stable working capital.

Mehdi Ennebati - ***Societe Generale - Analyst***

And in terms of working capital variation impacting the cash from operations, what should we expect for H2?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Svein Skeie?

Svein Skeie - ***Statoil ASA - Head of Performance Management and Risk***

Of course it's very much depending on where the market is going. As also Orjan is saying, it's that we have seen that there are benefits for then doing transportation of the crudes longer. So we have then sent, for example, some cargoes then towards Asia, meaning that they are longer on ship. And if those kind of markets continue then we will have more working capital. But if those markets change and shorter distances, that could mean that we could go down. So it would depend very much on the pricing structure as we are moving month by month going forward.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Yes. So you should expect also a correlation to prices going forward.

Mehdi Ennebati - ***Societe Generale - Analyst***

Thank you.

Operator

Michael Alsford, Citi.

Michael Alsford - ***Citigroup - Analyst***

Thanks for taking my questions. I've just got a couple, if I could. Hopefully you can update us a little bit more on the guidance you provided at Capital Markets Day regarding cash flow breakeven. You've clearly reduced your CapEx for 2016 and I'm just wondering whether we should still think about you breaking even in 2017 at $60 per barrel or do you think that actually is now much lower given the cost trends and CapEx trends that you're seeing?

And then more specifically on the international business, clearly loss-making and a drag on profitability still and I just wondered if you can provide an update as to where you're getting to in terms of your key objectives around onshore CapEx cost, OpEx cost to bring the breakeven of that business down more substantially and make that profitable at low oil prices? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Michael. First on the guidance of cash flow and the breakeven, what we said on the Capital Markets, we have no changes to the guidance. We are on track. So what we talked about at the Capital Markets is that we could be neutral at $60 in 2017 and $50 in 2018 and that still is valid. So no changes. When it comes to the international business, we are profitable in many of the key areas. It is obviously challenging on the current prices and prices realized in the second quarter. And, as you know, we are structurally more exposed to the oil price than the Norwegian business due to the historic cost and lower margin.

The adjusted earnings of minus $506 million is mainly due to the realized -- lower realized prices. And at the same time I think it's fair to say that 23% reduction in OpEx SG&A is a good response to attacking the costs on the workable elements. We have a cash flow from the international operations of $12.4 per barrel, and that is also indicating that this is a cash-generating business. The total cash flow from the operations of the international business is $683 million, but still loss-making at current prices.

Michael Alsford - ***Citigroup - Analyst***

Okay. Thank you for the update.

Operator

Halvor Nygard, SEB.

Halvor Nygard - ***SEB - Analyst***

Yes, hello. So on CapEx, you cut your CapEx guidance by $1 billion from $13 billion to $12 billion this year. And if we look at year-to-date CapEx, it is at $5.3 billion, which implies a run rate of $10.6 billion. Would you say that you've still got headroom for further CapEx reductions or will CapEx in second half of this year increase by more than 20% as you see it now?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Okay. Thank you Halvor. Year to date we just spent -- I think it's $5.4 billion, and you should expect higher activity during the year with the Sverdrup execution, starting the execution of Peregrino phase 2 and a potential activity with fracking in Bakken on the Eagle Ford, so the US onshore operation.

As we have said today, we reduce our guiding on the CapEx to around $12 billion, and that's our best estimate for 2016.

Halvor Nygard - ***SEB - Analyst***

All right. Thank you. And another question on production. Your Bakken production fell 11% sequentially in Q1 and then another 14% sequentially in Q2, while, if I remember correctly, you stated at Q1 that the drop in Q1 was not representative going forward. What are your plans for activity and production US onshore going forward?

Hans Jakob Hegge - ***Statoil ASA - CFO***

We still have one operated rig in each of the plays and in the second quarter a frack crew in Bakken in Eagle Ford. So Bakken production was reduced compared to the first quarter, with no wells completed in the quarter. So since the first-quarter prices have improved so we are considering picking up some activity in the second half, but cost focus remains critical.

Halvor Nygard - ***SEB - Analyst***

Okay. Thank you.

Operator

Tom Robinson, Deutsche Bank.

Tom Robinson - ***Deutsche Bank - Analyst***

Afternoon, everybody. Thanks for taking my questions. I've got two, if I may. The first one is on cash flow. Could you just help bridge the operating cash flow before tax and working capital from the first quarter of this year to the second quarter? I'm coming at this from the angle of if I look at the face of the cash flow statement, we've moved from roughly $3.4 billion to $3 billion in a quarter where pricing is a bit better, volumes are down marginally and the cost base is up slightly. So is there another factor I'm missing to explain the downward direction of cash flow quarter on quarter? That's the first one.

The second one just briefly is on CapEx. Would you be able to break out the $1 billion of savings in more detail? I appreciate $200 million or so is exploration, but how does the remaining $800 million split between the regions and the divisions? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Let me start off on -- first of all, Tom, thank you for those questions. Let me start off on the cash flow and then Orjan Kvelvane will fill in with more detail.

But in general the cash flow will vary over time with the level of volatility that we see. And the basis for looking at the cash flow I think is a robust cash generation, given the realized prices in the second quarter, with a strong operating momentum and a high regularity that we see. Cash flow from operations was $6.4 billion year to date. Given the significant reduction in the average liquids prices, it's the basis.

And then into more detail, Orjan.

Orjan Kvelvane - ***Statoil ASA - Head of Accounting***

So the way I understood your question was the second quarter towards the first quarter. And you're right, the adjusted earnings are up and the cash flow quarterly is down pre-tax and working capital. And as you know, this is about a kind of non-cash element and it will also be impacted by accruals and provisions that is both cash and non-cash. So this is a mixed bag of elements. But one example is over-/underlift where we, in the adjusted earnings, have a negative effect in the first quarter, a positive effect in second quarter. That has -- that will not impact any of the adjustments in the cash flow; that is based on the IFRS numbers and these are the adjusted numbers.

In addition, we have some financial element that also is part of the cash flow from operations that is not part of the adjusted earnings. So it's not easy to compare one to one, but this was some comments to enlighten you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

And then to the second question about CapEx and the $1 billion reduction, it is across the portfolio. And a material part of it is from producing fields, both operated and partner-operated. So it's difficult to say one or two specific reasons. But if you're highlighting one, it probably should be the continuous improvement in the drilling and wells. To take an example from the Norwegian Shelf that exploration wells in 2013 was drilled in 46 days on average, now down to 22 days. So overall I think it's fair to say strict prioritization, capital discipline across the Group.

Tom Robinson - ***Deutsche Bank - Analyst***

Thank you. Thanks for the detail.

Operator

Anne Gjoen, Handelsbanken.

Anne Gjoen - ***Handelsbanken - Analyst***

Thank you. When it comes to the second quarter, you have commented on higher gas volumes despite lower gas flexibility. But when it comes to gas flexibility, the way the market is developing; do you consider the gas flexibility as less than before going forward? And is it possible that you also could give some more color on the way you see the development in the gas market into 2012 -- 2017? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Anne. As you know, most of the increase is from associated gas production in the quarter. The flex gas comes from Oseberg, which was a bit lower than last year. So year on year the flex gas is lower. Going into your second question about the EU gas market, it's obviously a very interesting one. And the way we look at it is that the market is fairly well supplied in Europe at the moment. We see potential upside linked to the capping of the Groningen field. We see political willingness in relation to the climate agenda to be more in favor of gas as opposed to coal. Also we are aware of the indigenous decline that we have seen. So there are many factors. But at the moment it's well supplied. And, as I said, we probably expect to see some continued pressure on the prices short term. Longer term we have an optimistic view on the European gas market.

Anne Gjoen - ***Handelsbanken - Analyst***

Thank you.

Operator

Brendan Warn, BMO Capital Markets.

Brendan Warn - ***BMO Capital Markets - Analyst***

Yes. Thank you. Thanks for taking my question. It's Brendan Warn from BMO Capital Markets. Just first question of three I guess. The first one relates to the international business and you talked about impairments. Can you just talk through your future impairments and what we expect in the current forward curve or your current impairment tests? I notice that your DD&A has increased and the international business is still loss-making.

Second question. Just in terms of the MMP business, any guidance update you can give us just in regards of the change of conditions for the back end of this year, particularly with refining margins off and gas and oil pricing?

And then just last question. Just in terms of your debt maturity profile, can you give us a -- can you just talk about what you're looking at in terms of refinancing or payment down of your maturities, certainly in the next couple of years, please?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Okay. Thank you for those questions Brendan. When it comes to the impairment, we only had one impairment in the quarter. That was the Gulf of Mexico asset, not operated by ourselves. That was linked to a revision of the reserves. We use the forward prices, as you say, but after some quarters where we have done quite a few of these impairments we're only down to one this quarter. Last quarter you probably remember we had a reversal as well. So going forward, this will be based on not only the forward prices and price assumptions but also reserve revisions and the updating of business plans.

Then to the second question about the MMP business. On the guiding, there are no changes. We expect to see volatility and we are in this quarter within the range of $250 million to $500 million. And you should expect us to be within that range going forward.

When it comes to the debt profile, we have an average of nine years and no current plans on refinancing for 2016. So we have $16 billion in cash and the profile is so that we have $1 billion for this year, increasing to $2.5 billion next year and just above $3.5 billion in 2018. So the maturity or the profile is something we are comfortable with.

Brendan Warn - ***BMO Capital Markets - Analyst***

Okay. I appreciate it. Thank you.

Operator

Anish Kapadia, TPH.

Anish Kapadia *- TPH - Analyst*

Good afternoon. A couple of questions. Firstly I wanted to get an update on some of your projects and timing on potential FIDs on the Canadian offshore given your recent update, the BMC-33 project in Brazil, if you take over operatorship, and also Johan Castberg and Bressay.

Secondly, on your US assets, you've made a few disposals in terms of your north east gas position, and it's now largely non-operated. I was wondering if it's right to see this as a non-core position that could continue to be monetized.

And then finally on the midstream assets you've got in the US, I think you revealed about $1.5 billion of book value associated with those assets. What's the EBITDA that those assets generate and also potential to monetize these? Thank you.

Hans Jakob Hegge *- Statoil ASA - CFO*

Okay. Thank you, Anish. On the projects first, overall we are on track, both on cost and schedule. Let me just mention Sverdrup phase 1 which is into the execution phase, then Gina topside just has sailed from Korea. We have Mariner and we have the heavy lift today on Asta. And Mariner and Aasta has a planned sail-away scheduled for 2017.

You mentioned the Canadian offshore. Still being evaluated. We have done exploration campaign. We just finished a 19-month exploration campaign and we had two discoveries confirming the value range or volume range of 300 to 600 million barrels.

BM-C-33, we hope to get the consent on being the operator of BM-C, so that's the next milestone. We have agreed on Castberg with the partners on an FPSO concept as that's the most efficient one as we see it. And we discussed the FPSO involving shuttered tankers and the concept selection that DG2 is planned for autumn this year and a potential FID in 2017.

When it comes to Bressay, it's been postponed so we'll have to revert to that on a later stage.

And then on the US assets, talking about -- I think we have a strong position when it comes to US. We are placed in the good basins. It's a good acreage. We see costs coming down. And the main focus is on efficiencies. When it comes to M&A activity, we comment more specifically on that when the deals actually have taken place.

Anish Kapadia *- TPH - Analyst*

And on the midstream, the EBITDA from the midstream in the US?

Hans Jakob Hegge *- Statoil ASA - CFO*

We do not go very specifically into that part. It's seen as a part of the MMP business. And the guiding in that I just commented on, the 250 to 500, it is a part of that and we do not go into further detail at this point.

Peter Hutton *- Statoil ASA - IR*

Just before we go into the next question, in the interest of time, can I ask all questioners to keep it to a maximum of two questions each? I'll impose my normal rigorous discipline. Thank you. If we move over to the next question, please.

Operator

Oswald Clint, Bernstein.

Oswald Clint - ***Sanford Bernstein - Analyst***

Yes, thank you. Maybe a question on Johan Sverdrup. I don't think I've heard you comment on the volume increase that was talked about from Lundin. Maybe you could just talk about that 100,000-barrel-a-day increase that they're talking about. Is that something you will confirm or agree? Is that a press release type thing or is there still work being done on that initial plateau production level, please?

And maybe secondly on the drilling efficiency comments today. Is that -- so is this drilling faster? Can you talk about the days -- how many days to drill a well you've brought that down to, or is that actually the rate that's being paid per day? Maybe a little bit more color around that, please, would be quite interesting. Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Oswald. When it comes to Johan Sverdrup, we, as I said, we are well into the execution phase. The studies done on the processing equipment can confirm there is upside. But this is one of several factors impacting the production.

So when it comes to where we are with the milestones, the construction start of the living quarter platform at Aker Stord was at the end March. Steel cut on the riser platform. Top side at Samsung in Korea in June. And pre-production wells drilled to target that, finalized by end June.

And we are working closely with the partners on the phase II. And there is a concept select plans around year end, potentially early 2017. So when it comes to adding volumes, we have nothing more to add today.

Then to the drilling efficiencies, more color to that. We have a more standardized approach. Some of you might have heard about the perfect well concept that actually was developed on the US onshore business, where we went through the best performance of the various parts of not planning only planning but execution of various wells. And we combined it into a quite rigorous assessment of the well. So it's an upfront loading of the operations before it takes place. And you have to go through a practical checklist of at least 12 points that you have to check out that you are according to the best practice. And by doing that in a rigorous way, the execution runs not only faster, but cheaper. So on the exploration wells on the Norwegian shelf, we have been able to reduce the number of days on average from 46 to 22. So it's rigorous planning and discipline when it comes to the execution.

Oswald Clint - ***Sanford Bernstein - Analyst***

Great. Thank you.

Operator

Teodor Nilsen, Swedbank.

Teodor Nilsen - ***Swedbank - Analyst***

Good afternoon and thanks for taking my question. The first question is on dividend. Hans Jakob, you mentioned that 43% elected shares for the first-quarter dividend. Assuming that oil prices stay below $50 per barrel, will you then consider to increase the discount on the shares to encourage a higher portion taking shares as dividend?

And then my second question is on CapEx. Assuming that during 2017 you invest in only your sanctioned projects and also that prices stay flat from current level, should we expect 2017 CapEx to be below or above your updated 2016 guiding? Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Teodor. When it comes to dividend, we had a 43% take-up on the fourth quarter 2015. So we think that's -- we're happy with that, so we continue with 5% discount for the first quarter this year.

And if the take-up continues at this level, it will contribute with a 3% to 4% on the gearing at program end. And that's where we are at the moment. So no change to the discount. We keep the discount for the first quarter this year.

On the CapEx, I leave the word to Svein Skeie.

Svein Skeie - ***Statoil ASA - Head of Performance Management and Risk***

Yes. Thank you, Hans Jakob. When we look at where we are now, it's the $12 billion, as said. As we also say, is that for the second half of this year, we expect then to have some more CapEx compared with the first half due to the fact that we are then into more execution phase on the Peregrino phase 2 as well as the Johan Sverdrup. But also, we see that some projects are then put into production.

To us, as we said, we have the flexibility and we try then on the CMU, then we gave a guidance and then where we expect then to spend the CapEx going forward. Flexibility of $2 billion to $3 billion in the 2016 and 2017 and increasing further.

So then for next year, we are continuously evaluating where we are and the project. For new projects, if we then talk about that for next year, the main part of those will then come into the late part of 2017, so not impacting 2017 CapEx that much. Only this year we have the Trestakk and the Utgard, which are the new developments that we expect coming into play.

Hans Jakob Hegge - ***Statoil ASA - CFO***

So, Teodor, we will have to come back and be more specific on CapEx for 2016 at a later stage.

Teodor Nilsen - ***Swedbank - Analyst***

Okay. But just a follow up on the CapEx. Assuming that oil price stays at the current level, is it fair to assume that a higher portion of overall CapEx will be invested in Norway compared to international than we will see this year?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Too early to say. One of the dilemmas is, for instance, US onshore, where we have a frac crew in Bakken and Eagle Ford. So we don't run CapEx by the spot, we take a long term. And this is some of the things that we discuss on a more continuous basis, based on the market assessment in the various segments.

Teodor Nilsen - ***Swedbank - Analyst***

Okay. I understand. Thank you.

Operator

Thank you. We'll take our next question from Rob West from Redburn. Please go ahead.

Rob West - ***Redburn - Analyst***

Hi there. Thanks for taking my questions. I've got two, please. The first one is on the recent wage agreement that I think was announced with Norwegian workers over the course of the quarter. And maybe they're still even ongoing in some places. But the way that's been agreed, can you talk about -- do you still have the scope to improve the productivity of the way you use workers and labor and drive down costs on the Norwegian continental shelf from that?

And then secondly, this is a bit of a niche question about the cash flow. But I was wondering, could you comment about some of the specific one-offs that we can't see impacting the numbers in the quarter, and particularly around derivatives? Were there any payments against derivatives in the quarter? Just because I'm trying to back out of the cash flow statement that you reported. It looks as though there might have been a bit of a payment into that category. Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Rob. First, on the wage agreement, first of all we think it's good that we reached an agreement. We work closely with the workers and the unions on improving our business. This is one of the explanations why we have succeeded reducing the costs. 11% down on DPN per barrel on the OpEx SG&A. It's been a very positive trend over several quarters when it comes to reducing the cost. And we engage in a close dialogue with the workers on not only reducing their external services, doing more of the work ourselves, but also reducing the overtime spent. One of the reasons we have succeeded is because we have seen that we could plan better and do more the work ourselves and be aligned on the practical execution of the work. So that is good also that we have a wage agreement.

On the cash flow, Orjan, a bit more color? Specifically on the derivatives and MMP?

Orjan Kvelvane - ***Statoil ASA - Head of Accounting***

Yes, so there are derivative effects both from commodity derivatives and also financial derivatives. It's negative on the commodities side and positive on the financial side. So I would say that on the cash flow, on the specific elements, I would highlight maybe the collateral inflow, so close to $1 billion in cash inflow. And then of course hitting the financing activities. I think that is the main part that I would highlight.

Peter Hutton - ***Statoil ASA - IR***

Operator? Are we able to call for the next?

Operator

We'll now take our next question from Biraj Borkhataria from RBC. Please go ahead, your line is open.

Biraj Borkhataria - ***RBC - Analyst***

Hi. Thanks for taking my questions. I had a couple. Firstly, on exploration, you're 10% down on the budget. I was wondering if you'd talk about the level of activity there. What is the number of wells you're going to drill now versus the number you planned to drill at the start of this year? That would be my first question.

And the second question is on the US onshore. Could you just remind us what the CapEx that was spent in this business in the second quarter and what the full-year budget is for CapEx there? Thanks.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Biraj. First on exploration and the number of wells. Let me just take you through a quick update. We drilled eight wells in the second quarter. We have 15 year to date. I mentioned the 19-month drilling program, east coast Canada. That confirmed the volume of 300 million to 600 million barrel range, and we are maturing further prospects there. Two discoveries. We also had successful access, awarded five licenses in the 23rd round. Four as operator and the first well will be drilled in 2017. In terms of spending guidance, as you said, we reduced it by 10%, we see continued efficiencies. We also see that there will be a bit more activity going forward, more seismic in the second half. Around 20 wells for the full year. So that's the main point on exploration.

CapEx US onshore was very low in the first quarter due to hardly any fracking. One rig in each play. Expect to see a bit higher spend in the second quarter. Still at an activity level reflecting the current prices, which we cautiously call value over volume. So strict prioritization, main focus on costs.

Biraj Borkhataria - ***RBC - Analyst***

And could you just remind us what the full-year CapEx budget is for the US onshore business?

Hans Jakob Hegge - ***Statoil ASA - CFO***

We do not go into that level of detail, unfortunately.

Biraj Borkhataria - ***RBC - Analyst***

Okay. Thank you.

Operator

Thank you. We will now take our next question from Jon Rigby from UBS. Please go ahead.

Jon Rigby - ***UBS - Analyst***

Yes, hi. Thanks for taking the question. Just a quick one, a clarification on Canada. I think when you originally announced the Bay du Nord discovery, you said 300 million to 600 million and then that was after Mizzen and Harpoon. And I think you've made two further discoveries. So I'm just trying to square that with what you're saying about the 300 million to 600 million barrels that you have confirmed. Is that -- well, anyway, can you explain how that arithmetic works, please?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Yes. The discoveries, John, is Bay de Verde and Baccalieu. So they -- overall we could say that I'm a bit disappointed that we didn't prove even more volumes. Having said that, from the campaign, but due to the new discoveries we are still at the 300 million to 600 million barrels. So it's more confirming the range that we said prior to these discoveries. So we are working on further exploration potential in the area and maturing further prospects. We're also looking at a lean development solution on the Bay du Nord. So the timeline and the concept solutions are being reworked.

Jon Rigby - ***UBS - Analyst***

Right, but that range is enough critical mass to support the development, is it? In your current thinking?

Hans Jakob Hegge - ***Statoil ASA - CFO***

In terms from our potential FID decision, that will be based on not only the volumes and the confirmation of those, but also the lean development solutions and the cost attractiveness of that. So it's a bit early to conclude.

Jon Rigby - ***UBS - Analyst***

Okay. Thank you.

Operator

Thank you. We will now take our next question from Anders Holte from Danske Bank. Please go ahead, your line is open.

Anders Holte - ***Danske Bank - Analyst***

Good afternoon, gentlemen, and thank you for taking my quick questions. So the first one relates to the cash flow for the quarter before taxes and working capital, as earlier mentioned. I think we're all pleasantly surprised by the Q1 result at $3.4 billion. And now we're down to $3 billion despite hiking prices that's been throughout the quarter. So a question then, is this the level that we should expect if prices remain unchanged for the remainder of the year?

And second question is related to your spoken positive view on gas prices in mainland Europe. And how much of that is tied up to and expecting higher pricing of carbon, which I guess is a prerequisite for starting to retire the brown coal power plants in Europe. Thank you.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Okay. Let me do the first question and then Svein takes the second one.

So the results reflect the current commodity prices, no doubt. But cash is very much in line with what we said at the CMU. We have the maintenance seasons and the costs associated with that. That will be higher in the third quarter. Remember we have the underlying production growth and we see the costs coming down. And we are making our portfolio even more robust, with lower breakeven levels. And also going forward, the market effects will increase as we reduce the service cost in 2017 and 2018.

At the CMU, we showed a graph indicating around $10 billion in annual average cash flow, at $40 for 2016, 2017. And the cash flow from operations in the first half of 2016 has been $4.1 billion at slightly below $40, which is lower than the run rate suggests. But keep in mind that the cash tax payment in the first half is based on the results from 2015 and does not reflect the $40 per barrel we saw in the first half. So cash tax was almost $700 million higher in the first half than on adjusted earnings. Also, at flat prices, the cash flow from operations should be higher in 2017 than 2016 as we will have higher production next year.

Svein, the second question goes to you.

Svein Skeie - ***Statoil ASA - Head of Performance Management and Risk***

Yes. Thank you. Regarding then the gas outlook, as Hans Jakob explained a bit earlier, on the outlook going forward. In the shorter term, there are gas then coming then into Europe. But still, if you look at the indigenous production, the Groningen field, it's going down.

Going forward, also then based on the Paris discussions that we had, there are expectations then for Europe then to do something with the carbon emissions. And in such a context, pricing on carbon, in one way or another, will probably then be an efficient measure to do it. So what we expect is that going also forward, based on the agreement that we had in Paris, we should expect that there will be more pressure then to take out coal with high CO_2 emissions.

And then gas is very well placed to replace it. And since we have the pipeline in place and we have the field in place, we have very competitive gas that could supply Europe with new gas also going forward.

Anders Holte - ***Danske Bank - Analyst***

Thank you. That does it for me.

Operator

Thank you. Our next question comes from Josh Stone from Barclays. Please go ahead.

Josh Stone - ***Barclays - Analyst***

Hi, good afternoon. I've got two quick questions, please. Firstly, on efficiency. Are you able to say what's been achieved already versus the $2.5 billion efficiency target from February? And secondly on gas deferrals. Are you able to say what the production impact was during the second quarter? Thanks.

Hans Jakob Hegge - ***Statoil ASA - CFO***

Thank you, Josh. On the efficiencies, it's very encouraging to not only state that we started early, prior to the drop in oil price, but also that we've been able to increase and double the efficiency gains over the time. So we're not changing the guiding on the $2.5 billion. It's still valid and we are running according to plan.

Several encouraging areas to pick on the specifics. I have mentioned already the drilling and well. We see that on the US onshore operations, even if the activity has been taken down, the efficiency is increasing. The service cost has also been partly covered in this call, but relatively limited effect. Still valid at $300 million to $400 million in 2016. But going forward, I think it's definitely a higher potential when it comes to the service cost and the effect of that as the new projects are being sanctioned. And last but not least, on the OpEx side, we see the MMO contracts on the modifications and maintenance on the Norwegian shelf. That was implemented in April.

The implementation period will go on to the end of October this year. And in the transition period, you could also actually see a bit higher costs short term, when you change from one company to the other. But my experience from the operations is that when the wheels start turning with the new players in there, you would definitely see more efficiency.

So the $2.5 billion is still valid. Remember that when we reduced activity, the basis for doing the improvements is also decreasing. So it's not purely about the activity level, it's also about the basis you are improving from.

On gas deferrals, Svein?

Svein Skeie - ***Statoil ASA - Head of Performance Management and Risk***

Yes, on -- in this quarter, compared with then last year, there was a slight reduction that we did then on Oseberg field, but not a major thing. We are following the market very closely, how it develops, and looking at the structure in the market. And then, since we have the flexibility, we also have the flexibility if the market opportunity is there, to defer gas if that makes value, because we are focusing on the value side of it, not the volume side of it.

Josh Stone - ***Barclays - Analyst***

Great. Thanks very much.

Operator

Thank you. We will now take our next question from Hamish Clegg from Bank of America. Please go ahead.

Hamish Clegg - ***BofA Merrill Lynch - Analyst***

Hi. Good afternoon. Thanks, guys. Just first of all revisiting the cash flow comments you made earlier, and that capital markets day slide that very usefully outlines CFFO versus CapEx at the different oil prices. As you said, the cash tax element was slightly, let's call it, back-end-loaded. Could you maybe tell us if you feel entirely comfortable with that approximately $10 billion of CFFO for the full year?

And with that in mind, what's the impact of the swap-out of Edvard Grieg in the second half? And how will that impact that number or will it not?

And then my second question, very simply, US gas prices obviously made a bit of a recovery towards the end of the quarter. And although I know they were down slightly in the quarter, can you tell us if you think you'll be capturing these higher gas prices going forwards, because my back-calculated gas realization suggested that you were probably making slightly lower US gas realizations than I'd expected. Is there some hedging involved in that?

Hans Jakob Hegge - ***Statoil ASA - CFO***

Okay. Thank you, Hamish. First on the cash flow and CMU. Yes, we are comfortable with the $10 billion in cash flow from operations at $40 per barrel. This is for 2016 and 2017, not only 2016. So will be higher next year due to taxes and production growth.

On the impact from Edvard Grieg, yes, this will have an impact along with other portfolio adjustments we have done. So that's the short answer to your second question. But as you know, we don't generally update the guidance after individual transactions.

Hamish Clegg - ***BofA Merrill Lynch - Analyst***

Okay. So we'll wait for next year's Capital Markets Day for a change on that? Or will you be giving us some guidance on Edvard Grieg, how we should account for that in our modeling?

Hans Jakob Hegge *- Statoil ASA - CFO*

Well you know the direction.

Hamish Clegg *- BofA Merrill Lynch - Analyst*

Yes, we do. Thanks.

Operator

Thank you. We'll now take our final question from Nitin Sharma from JPMorgan.

Nitin Sharma *- JPMorgan - Analyst*

Thanks. Afternoon, everyone. Just a quick one. Hans Jakob, when you think of the three key objectives, organically covering your dividend, investing for future growth, improving reserve life and finally gearing, how do you think about balancing those three objectives in terms of the decisions that you take this year and next, please?

Hans Jakob Hegge *- Statoil ASA - CFO*

Thank you for that question. I think it's fair to say that we take a long-term perspective on our business and balancing this. On the dividend, we've said it's important. We confirm that today by maintaining at the same level, continuing to pay dividend and continuing with the scrip, offering the 5% discount.

We focus on the fundamental improvements. We think it's very important to address the cost and efficiency issue that has been seen not only this year but over a period of several years. So we continue to invest in high-quality projects, ensuring that these are as good as they can at the point of the FID. Mainly two elements in the decision. Can we improve further on the concept, on the economics. And if not, we should sanction it if it's a robust project going forward. Also what do we think about the timing in the market with the capacity and the supplier industry and the rates offered.

And we do this within a strong financial framework. We have a stable outlook on the credit rating. We are comfortable with the current gearing level and we have $16 billion in cash.

Nitin Sharma *- JPMorgan - Analyst*

At what level of gearing -- if I may ask as a follow-up, what level of gearing does that strong credit rating come under question mark? Or is there a gearing level at all?

Hans Jakob Hegge *- Statoil ASA - CFO*

The ambition level on gearing is to stay over time between the 15% and 30%. But when we cross the line, as we did in this quarter, it is in line with the guiding we did at the CMU. And we said this is expected at the current prices. We have a more optimistic view on the market long term. So we think we will have a recovery of the prices. We see some signs that we are moving towards a more balanced market, maybe 2017. And then we will eat of the high storages and we'll probably see a more normalized situation, where geopolitics and things like that would affect the prices and have a positive response on that.

So the long-term perspective with value over volume and quite stable outlook is important to us when we make these decisions.

Nitin Sharma *- JPMorgan - Analyst*

Thank you.

Peter Hutton - ***Statoil ASA - IR***

Thanks, everybody. That's the end of the questions and for the presentation. Thanks for joining us today. As ever, if there's any follow-up questions, please don't hesitate to call the investor relations team.

And with that, I'll wish you the best and we'll be calling again in the future. Thank you. Bye-bye.