PJSC "LUKOIL"

2019 Results

Conference Call and Webcast Transcript

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Pavel Zhdanov

Slide 3

Good afternoon, ladies and gentlemen. Thank you for joining us today for this conference call on LUKOIL's results for 2019.

We will start with a presentation and then move on to a Q&A session.

I would like to draw your attention to the fact that the presentation contains forward-looking statements that are based on our estimates, assumptions and expectations. More detailed information is presented on the slide.

Now I would like to hand over to Mr. Vagit Alekperov, President and CEO of LUKOIL.

Vagit Alekperov

Slide 4. Title (Interim Results of Strategy Implementation)

Thank you, Pavel. Good afternoon, ladies and gentlemen.

I realize that you are primarily focusing on the current situation, but I'll start with last year results.

Slide 5. Operating results: outpacing strategic targets

2019 was the second year of executing our long-term strategy that we unveiled in early 2018. Despite the high volatility of the external environment, we delivered excellent results with new highs reached in some areas.

Our operating results were ahead of the strategic targets. In particular, hydrocarbon production exceeded the minimum target by 2.5 times on average, even despite external limitations. In the refining segment, we were well ahead of the plan to reduce the output of high sulfur fuel oil on the back of the hike in throughput volumes.

We were able to achieve both a quantitative and qualitative increase in all business segments, most of it organic. This result is fully in line with the core strategic goal of unlocking our existing potential.

I would also like to highlight significant progress LUKOIL is making in developing and scaling up efficient technological solutions in the upstream segment, which enables us to boost our reserves and production potential.

Slide 6. Financial results: an all-time high

We made great progress in our efforts to improve efficiency and optimize costs. Controllable costs per barrel decreased by 5% compared to 2017. As a result, many of our cost items went down to the 2016 level. We have also strengthened our capital reinvestment discipline.

Thanks to our work, in 2019 we achieved record high financial results and, most importantly, the return on capital of 15%. I consider this an excellent result, especially compared to our international peers.

On top of that, thanks to conservative planning, we are able to maintain a very strong financial position, which makes us flexible and allows us to move forward in the face of volatility.

Slide 7. New capital return policy: shareholder distributions growth

As you are well aware, we have always treated capital distribution to shareholders with utmost responsibility. Last year, we made an important decision on this matter, which was based on a detailed analysis of external and internal factors.

We introduced a comprehensive and efficient solution in the form of a new policy that envisions paying 100% of free cash flow in dividends and a shift to opportunistic share buybacks. This approach means higher returns for shareholders and more flexibility for the Company in terms of our reinvestment capacity, as well as a better capital structure and a balanced shareholder structure going forward.

The new policy carries a strong advantage such as the complete transparency of dividend calculations. For instance, based on last year's accounts, the estimated dividend amount stands at 542 rubles per share. This is more than two times higher compared to 2018 dividends.

As a reminder, in 2019 we also distributed a significant portion of the capital by buying back shares. This was equivalent to dividends of over 350 rubles per share. In other words, the total capital distribution for 2019 on a per-share basis may reach nearly 900 rubles.

The Board of Directors will decide on the recommended dividend amount in the second half of April.

Slide 8. Sustainable development: system approach, continuous improvements

As the global and investment communities are becoming more conscious of sustainability issues, we make sure to keep our finger on the pulse and address any stakeholder concerns in a timely manner.

I would like to emphasize that ever since LUKOIL's foundation, we have been exercising a systemic approach to managing sustainable development aspects and consistently improving our performance in this area. In particular, new functions recently delegated to the Strategy and Investment Committee have strengthened the Board's role in sustainable development stewardship.

The Company implements targeted programs along a number of lines, which result in continuous improvement of key sustainability indicators.

Some of the most important achievements of the recent years include a significant decrease in the number of workplace injuries among contractor personnel working at our facilities, as well as an increase in the use of associated petroleum gas to an all-time high of over 97%.

LUKOIL is delivering excellent performance in combating climate change – one of the most important issues on the global agenda currently. Since 2016, we have reduced direct greenhouse gas emissions across our Russian assets by 3% – far ahead of the target. As part of the forthcoming update of the long-term strategy we plan to give a special attention to be placed on the climate issue.

Slide 9. Positive free cash flow in any price environment

A few words on current market developments.

To begin with, it is yet difficult to predict how prices will perform in the oil market. The market is currently driven by emotions as no one has expected such drastic supply-side changes. There is also another strong, but hopefully temporary, factor on the demand side in play and that is the coronavirus outbreak.

This is not the first time we see a drop in oil prices. In effect, we have got used to high volatility and have many years' experience of overcoming challenging times. Yet, we were able to keep free cash flow positive and continued robust development. Our resilience was supported by a whole range of internal and external factors.

Furthermore, we have improved our operational performance significantly over the past years. Our net debt is close to zero, we maintain rigorous control of costs and have a highly flexible financial policy.

All this makes us even more prepared for lower oil prices than we were five years ago. And I am confident that we will be able to successfully make our way through the price cycle and aim to continue delivering sustainable business growth well into the future.

Thank you.

Now I would like to hand over to Azat Shamsuarov, Senior Vice President for Upstream.

Azat Shamsuarov

Slide 10. Title (Upstream)

Thank you, Vagit. Good afternoon, ladies and gentlemen.

Slide 11. Upstream strategy

Over two years of implementing our Upstream Strategy, we have reached great results and exceeded our plans and expectations on almost all counts.

As you know, since 2017 up until recently we have been operating under external limitations on oil production in Russia. Additionally, in 2019 we saw limitations in gas intake from Uzbekistan projects. Still, we managed to exceed our hydrocarbon production targets. For example, production growth in 2019, excluding the West Qurna-2 project, reached 1.4% versus the initially planned 0.5%. Over the two years, our production increased by more than 5%.

Following our value-over-volume principle, we continued focusing on the priority projects. The share of high-margin barrels in 2019 grew to 32%. This makes for an increase of more than 10 percentage points in two years. As a reminder, our strategy envisions reaching the 30% level only in 2020.

In addition to better production mix, we also achieved improvements in business efficiency through cost cutting coupled with development and roll-out of technologies.

This combination of factors results in higher growth of the segment’s financials relative to the production growth rates.

Slide 12. West Siberia

We were able to bring down the production decline at mature West Siberia fields from 10% in 2016 to 2.5% in 2019. Were it not for the external production limitation, the 2019 figure would have been even better. Originally, we planned to reach the rate of 2-3% no sooner than 2020 and with no external limitations.

As part of the strategy update, we will pay particular attention to analyzing our mature field opportunities, but it is already quite clear that there is significant potential to improve the production profile.

This comes mainly on the back of the efficiency improvements already achieved through the scale-up of technologies and cost cutting.

Slide 13. Increasing efficiency via technology development and scale-up

In 2019, we almost doubled the number of horizontal three-string wells, which are a more basic version of the standard well and are on average 20% less expensive. On top of that, we were able to bring down the cost of drilling three-string wells by 8% compared to 2018. You may remember that we drilled our first basic multi-bore well in 2018. By the end of 2019, 20 such wells had been drilled. We continue to work on removing technology-related restrictions in order to apply this solution on a wider scale.

Compared to 2018, the number of small-diameter wells went up by 1.5 times. These wells are 50% less expensive than standard directional wells. This year, we plan to double their number. This means that we will be rolling out such wells at a much higher rate to what was previously planned.

We have also increased the share of complex wells in West Siberia to 44%, or by 11 percentage points compared to 2017. These wells are effective when it comes to highly complex deposits. The technology is being constantly refined, making this solution cheaper. For example, the cost of drilling multi-bore wells decreased by 4% year-on-year. It was achieved thanks to a 13% increase in the speed of drilling.

In the future, the speed of new well construction will also be boosted through the roll-out of batch drilling, which has been successfully piloted at several of our fields.

We are actively developing digital technologies in production. The intelligent field concept that relies on integrated models is already being applied at 45 LUKOIL fields, which account for over one fourth of our production volumes. The application of neural networks to manage production and flooding at the pilot sites of mature fields has proven highly efficient. We plan to roll out this technology.

In addition, we are continuing to expand the use of energy-efficient pumps delivering more than 10% in electricity cost savings.

Slide 14. Cost reduction ahead of targets

By decreasing operating and capital expenditures, we unlock new opportunities to bring more reserves into production in an efficient manner. We implement targeted cost reduction programs.

In a number of areas, we exceed even some of our more ambitious targets compared to the ones set out in our Strategy in 2018.

In particular, over a two-year period we achieved a 8% decrease in per unit drilling costs. Construction costs remained flat compared to 2017, while lifting costs decreased by 4%.

We make use of an entire set of cost optimization tools, and in 2019 we decided to create a continuous improvement system that will bring an even sharper focus on enhancing efficiency.

Slide 15. Tax on additional income (TAI)

In 2019, we started the implementation of new development plans for the areas under the TAI regime. The total liquid hydrocarbon volumes produced at these areas during 2019 amounted to almost 5 million tons, or 6% of our total output in Russia. The investments exceeded 30 billion rubles, which is almost two times higher than the Company’s average on a per barrel basis.

In 2020, we plan to ramp up our respective capital expenditures to over 50 billion rubles. Compared to our plans before the introduction of the TAI, there will be almost 170 billion rubles of additional investment in these projects over the next five years.

The TAI effect is most evident for the third group of projects. These are mature fields in West Siberia. We increased drilling operations there by more than 20%, with production having grown by over 7% compared to 2018. I would like to emphasize that we are far ahead of the production target with the third group. The TAI scheme gives new life to our mature fields, transforming them into growth drivers.

Now I shall move on to specific regions and projects.

Slide 16. North Caspian

In the North Caspian, we have increased oil production by 7% year-on-year through our continuing development efforts at the Yu. Korchagin and V. Filanovsky fields.

In late 2019, we launched Phase 3 development at the V. Filanovsky field, bringing our construction program there to a close. In 2019, 5 wells were drilled in the field. We plan on further drilling of the well stock and maintaining an oil-rate plateau of 6 million tons per year.

We carried on with the drilling program on the Yu. Korchagin field. In 2019, we commissioned 4 production wells there and produced more than 20% above the 2018 volumes.

We were able to accelerate the Valery Grayfer field development and now plan to launch the production in 2022, a year ahead of plan. The ice-resistant stationary platform is already 35% complete, the platform for the living quarters – more than 60% complete. This year we plan to install offshore jackets for both platforms and lay the pipelines to the V. Filanovsky field.

A few words on our projects in the Baltic Sea. In May last year, we launched production at the D41 field. The field is being operated from the shore with two horizontal wells more than 7.5 thousand meters in length each. This arrangement allowed us to achieve much lower development costs and a much faster launch. As for the larger D33 field, project design works are underway, with the final investment decision expected at the end of this year.

Slide 17. Hard-to-recover reserves

We have been able to achieve significant volumes of production from hard-to-recover reserves. At the key fields, production grew by 1.5 times over the two-year period. In particular, the high-viscosity oil volumes increased by more than 40%.

We are continuing to expand our infrastructure and production facilities to produce more high-viscosity oil. At the Usinskoye field, we see potential to increase the plateau rate as compared to the current target thanks to new geological information and improved technology.

Our production at the largest low permeability fields increased by almost two times. Such an impressive result came on the back of the scale-up of unique technology and individual approach to each well.

Our success in developing the Sredne-Nazymskoye field in West Siberia with low permeability deserves special mention. In 2019, we increased oil production there by more than 1.5 times to 300 thousand tons, with more untapped potential still ahead.

In 2019, we continued working on transferring our tight oil reserves to a category where investment incentives apply. By the end of the year, we transferred over 47 million tons of reserves, which is two times more than in 2018.

Slide 18. Gas projects in Uzbekistan

In 2019, LUKOIL's share of gas production in Uzbekistan rose by 7% year-on-year to 14 billion cubic meters. The second quarter of 2019 saw limitations in gas intake from the Gissar project by the Shurtan gas processing plant as a result of unscheduled repairs. The production at Gissar was back to the target level in the fourth quarter of 2019. We were able to offset the unscheduled losses at Gissar with additional volumes from Kandym.

In Uzbekistan, we aim to preserve the current plateau rate, optimize maintenance capital expenditures, and assess the oil and gas bearing capacity of new investment blocks in the north of the Republic.

Slide 19. Acquisition of new international projects in accordance with the strategy

In 2019, we acquired stakes in the Marine XII project in the Republic of Congo and the Ghasha project in the UAE. These acquisitions are fully in line with our M&A strategy. The projects boast explored reserves and substantial production potential while also fitting our technological expertise.

For Marine XII, production is already underway at two fields. The current rate is approximately 40 thousand barrels of oil equivalent per day. We have recently launched the second phase of Nene development that includes the construction of a wellhead platform and drilling of 7 production wells. The preliminary design work for the third phase is already underway.

To finish my presentation, I would like to mention our success in overseas exploration projects. At the end of 2019, we drilled the first exploration well at Block 10 in the Gulf of Mexico, which resulted in the discovery of an oil field whose geological reserves, according to preliminary estimates, amount to 200 million barrels.

Thank you. Now I would like to hand over to Mr. Vadim Vorobyev, First Vice President for Downstream.

Vadim Vorobyev

Slide 20. Title (Downstream)

Thank you, Azat. Good afternoon, ladies and gentlemen.

The downstream segment not only markedly contributes into the Company’s free cash flow, while is also an important factor of sustainability of LUKOIL financial results during highly volatile times. The high level of vertical integration and high quality of our downstream assets gives the huge advantage to the Company during the periods of oil price weakness.

Slide 21. Refining strategy

As a reminder, our Strategy in the refining segment covers three key areas.

First, it is ongoing efficiency improvements at our existing facilities and optimization of maintenance CAPEX.

The second area includes selective projects to improve the product slate.

The third area focuses on petrochemicals production using our own feedstock.

Let me start with our performance in the first area.

In 2019, the refining throughput at our facilities rose by more than 2%. The growth was somewhat below our guidance as we optimized capacity utilization at our refineries throughout the year in response to the market environment to maximize our financial result.

At the same time, we were ahead of our targets in terms of improving the product slate, with the light product yield going up by 2 percentage points year-on-year.

Here I would like to stress that with a set of measures we had carefully developed in advance, the Company was able to reduce the yield of high sulfur fuel oil to a record low of 8% by the end of 2019. This helped to mitigate the negative impact that refining margins felt from the worsened spreads for high sulfur fuel oil. As compared to 2017, total output of fuel oil declined by more than 1.5 million tons.

Slide 22. Efficiency improvement program at refineries

Efficient refining is our key priority. We are committed to reducing costs and optimizing processes in order to enhance the free cash flow.

All our refineries have three-year operational efficiency roadmaps in place, which are updated on an annual basis. They include a range of comprehensive operational measures that either require zero investments or have very short payback periods.

Over two years, these initiatives produced an effect of more than 60 billion rubles. Of this amount, over 10 billion rubles comes from cost savings. This is strongly above our expectations.

In 2019, two of our refineries underwent a holistic review by external experts to identify additional opportunities for efficiency enhancement. This translated into a range of measures that had not been covered by any earlier roadmaps. We are planning to have the initiatives rolled out across the Group's other refineries and expect these efforts to deliver a sizeable additional impact.

On top of that, in 2019 we embarked on 23 pilot projects as part of the Digitalization Program at our refineries. The most successful projects will also be rolled out and are expected to deliver a further upturn in efficiency.

Slide 23. Selective projects at Russian refineries

As part of the Strategy's second area, we keep implementing selective projects at our plants.

The construction of a delayed coker in Nizhny Novgorod is now 60% completed. Pipeline installation and equipment hook-up works are underway. More than 70% of the equipment has been delivered to the site. The largest of our selective projects, it is designed to drastically reduce the output of fuel oil and increase the yield of light products.

At the same refinery, we are constructing an isomerization unit to increase the output of high-quality gasolines. The project is now 60% complete.

The other two projects focus on developing our premium businesses.

Our bitumen expansion plans at the Nizhny Novgorod refinery will help us to deliver on our strategy for the bitumen production. The result will be improved quality and output, including those of polymer-bitumen binders. We successfully completed a state environmental review, with part of the process equipment already delivered to the site.

The deasphaltizing unit at the Volgograd refinery will contribute to improved quality of lubricants and reduced production costs. The project completion rate has now exceeded 40%, with more than 40 units of equipment already installed and rack reinforcement and installation currently ongoing.

Slide 24. Product slate improvement amid MARPOL

Given the impact of MARPOL on price spreads, reducing fuel oil output is highly important. The market is searching for a state of balance, with new equilibrium levels hard to forecast as of yet.

On our part, we are doing everything we can to optimize the product slate and secure additional benefits from the current market conditions. As one example, last year our Volgograd refinery started producing marine fuel with 0.5% sulfur content, its annual capacity standing at up to 1 million tons.

In 2020, we expect to deliver fuel oil output at a level of below 8%. Thanks to additional measures we have been taking, this is better than our last-year guidance.

The launch of the delayed coker in Nizhny Novgorod will bring the fuel oil yield down to below 4% by 2022, which translates to less than 3 million tons of fuel oil annually. Some of our refineries will continue processing purchased fuel oil, which will take the balancing production volume even lower.

Slide 25. Growth projects in petrochemistry

As part of our strategy to produce petrochemicals at refineries using our own feedstock, we have made considerable progress in terms of designing potential projects.

Our focus is on projects to produce polypropylene at the Nizhny Novgorod refinery and the refinery in Bulgaria. These projects are now at the FEED stage. They are based on the propylene feedstock coming from catalytic cracking units.

We continued exploring potential construction of a global-scale pyrolysis facility using naphtha and LPG from our Russian refineries. After a thorough review of logistics, we have now selected the venue for this optional project. It is the Perm refinery, where we see the greatest synergies.

We have a number of strong competitive advantages enabling us to go ahead with petrochemical projects, and our key goal at the current stage is to analyze everything as carefully as possible, firstly marketing risks, amid continuously increasing level of global competition.

Slide 26. Filling stations

Now let us move on to product sales.

In the retail segment, the focus of our strategy is on improving efficiency and maximizing free cash flow.

We continue optimizing and upgrading our chain of filling stations with an emphasis on the geography and format of the stations. We are increasing the share of filling stations with non-fuel marketing space in the most attractive locations, while reducing the number of low-margin stations.

Work is ongoing to enhance efficiency and cut down on per unit costs.

Sales of non-fuel goods and services are demonstrating a double-digit growth. In two years of the Strategy implementation gross profit from this business has risen by almost a third, already covering over 40% of operating expenses at our filling stations with non-fuel marketing space.

Slide 27. Refined products logistics optimization

I would like to specifically highlight our achievements in optimizing motor fuels logistics. In 2017, we started exporting diesel fuel from the Volgograd refinery and supplying gasoline from the refinery in Nizhny Novgorod to the Moscow area using new trunk petroleum product pipelines of Transneft. In 2019, those supplies came close to 6 million tons, which is more than a 20% increase above 2018. Using data on logistic routes provides us with considerable savings in terms of transportation expenses.

Slide 28. Aircraft fueling and marine bunkering

We successfully moved on with our strategy in aircraft refueling and marine bunkering, which is aimed at maintaining our market share while also increasing sales to end consumers and improving efficiency.

Over the past two years, we managed to grow volumes of high-margin into-plane refueling by 16%, partly owing to stronger presence in Russian airports.

In marine bunkering, we maintain our market share in accordance with our strategy while also increase sales volumes in the high-margin retail channel.

Slide 29. Lubricants and bitumen

We see strong growth in our business of lubricants production and sales. Over the past two years, sales of our high value-added lubricant range increased by more than 20%.

As part of business development last year, we expanded our production by launching a new plant in Kazakhstan with a capacity of 100 thousand tons. This is a major milestone towards expanding our sales geography to the Asian market. In this area in 2019, we won a tender for service fills for Volkswagen and became the supplier of first fill for Daimler in China.

We continue to develop the strong potential of our polymer bitumen business. Here we are establishing the entire supply chain from production to end consumers. Last year, sales of bitumen to the road building industry grew by 1.5 times. Our total bitumen sales were close to one million, which is a 15% increase year-on-year.

Thank you. Now I would like to hand over to Mr. Alexander Matytsyn, First Vice President for Economics and Finance.

Alexander Matytsyn

Slide 30. Title slide (Finance: record results)

Thank you, Vadim. Good afternoon, ladies and gentlemen.

Slide 31. Macro environment

In 2019, the macroeconomic environment was less favorable for the Company's financial performance than a year earlier. A decline in average annual oil prices was only partially offset by the weaker ruble. Also, the past year delivered one of the decade's worst results in refining margins, following low gasoline spreads and a plunge in spreads for fuel oil at the end of the year. Additional pressure on refining margins in Russia came from increased excise rates for petroleum products.

The fourth quarter was also relatively unfavorable in terms of macroeconomics as oil prices and refining margins were going down while the ruble was getting stronger.

Despite the weak market environment, we delivered a record-breaking financial performance in 2019. This was driven entirely by business-related factors, including better metrics in terms of volumes and quality, strong vertical integration, and strict cost discipline.

Slide 32. Leadership in efficiency

In terms of key financial metrics, we were ahead of many of our competitors. This enabled us to solidify our leadership in efficiency compared to Russian companies and to considerably outperform a lot of majors.

Our free cash flow per barrel exceeded 12 US dollars, which is a new all-time high.

This is the best evidence that our focus on business development and efficiency improvement is paying off.

Now let me talk in greater detail about our 2019 financial results.

Slide 33. Revenue

The impact of lower prices on revenue from oil sales was almost fully offset by growing volumes of production and global trading.

Revenue from gas sales went up significantly as a result of increased production and higher prices.

Revenue from oil product sales declined on the back of lower prices in global markets along with reduced trading volumes.

As a result, total revenue was down by 2% year-on-year. The reduction in revenue was offset by ruble devaluation.

Slide 34. Cost control

We are delivering strong performance in cost optimization and control. As we have been stating previously, these efforts are our priority and a key tool to implement our strategy.

You may remember that two years ago we carried out a detailed review of the core expense items under our control and developed and launched targeted initiatives to improve efficiency. At the outset, our goal was to contain cost growth within inflation, but a year ago we focused on more ambitious objectives of keeping costs flat.

Our actual results turned out to be even better than the revised targets.

Conditionally controllable operating and administrative expenses per barrel went down by 5% compared to 2017 in nominal terms and by 12% in real terms. This means that in 2019, actual savings vs the scenario of cost growth in line with inflation exceed 50 billion rubles. Importantly, this amount does not include the effect of CAPEX optimization, where we also delivered some very strong results.

Let me stress here that efficiency improvement and cost savings not only help grow the Company's current free cash flow, but also open up new investment opportunities in the Russian upstream segment.

We plan to continue these very important efforts and, as Mr. Vagit Alekperov said, will be conducting an additional review of this area when updating our strategy.

Slide 35. EBITDA

In 2019, EBITDA reached a record high of 1.2 trillion rubles, going up by 11% year-on-year.

The strongest contributor to the EBITDA growth was the Russian downstream segment, driven by higher refining volumes, improved product slate, and better results in the retail segment.

Despite lower refining margins, downstream EBITDA outside of Russia improved on the back of a higher trading margin, positive effect of inventories at refineries, and higher refining volumes and improved product slate.

EBITDA in the upstream segment went up despite weaker oil prices. In Russia, the growth is attributable to a larger share of high-margin barrels in the structure of production, introduction of the TAI, and ruble devaluation.

Stronger upstream EBITDA outside of Russia is due to higher volumes of natural gas production.

Slide 36. Profit

Net profit went up by 3% in 2019 to 640 billion rubles. The increase is driven by stronger EBITDA and was constrained by higher depreciation on the back of production facilities commissioned in the Caspian Sea and Uzbekistan.

Another constraint was the reduction in non-cash foreign exchange gains, which is due to both FX rate dynamics and changes in the net monetary position in foreign currencies.

Slide 37. CAPEX

We are committed to a stringent investment discipline and are engaged in ongoing optimization of our capital expenditures.

Compared to 2018, capital expenditures stayed almost flat at 450 billion rubles.

In the upstream segment, lower expenditures in Uzbekistan and the Caspian Sea following the completion of the main construction works were offset by a rise in investments in West Siberia as a result of the introduction of the TAI regime and increased drilling operations at mature fields.

In the downstream segment, capital expenditures remained virtually unchanged year-on-year. The construction of a delayed coker in Nizhny Novgorod remains our largest project.

The share of the upstream segment in capital expenditures totaled 80% for 2019, with the share of expenditures in Russia exceeding 80%, which is generally in line with our strategic targets.

Slide 38. Sources and uses of cash

In 2019, free cash flow exceeded 700 billion rubles, or 10 billion US dollars. This is an all-time high for LUKOIL.

This was made possible by our unwavering focus on capital discipline that does not in any way compromise the financing for business development.

Our investment needs have been fully covered in line with strategic objectives but taking into account the OPEC+ restrictions. No external limits on production would mean a larger investment program and a smaller free cash flow.

Let me also point out that in 2019, we fully honored our capital distribution commitments to our shareholders in line with our previous policy. Dividends for 2019 are now regulated by the new policy taking into account that, in 2019, a considerable amount of capital was distributed through a share buyback program.

A major decision we made as part of reviewing our capital distribution policy is the transition to debt financing of our M&A deals. This move will help further improve the Company's capital structure.

I would also like to say a few words on the share buyback. As you know the 3bn US dollars buyback program is in place. In line with the new capital distribution policy we consider buyback as an opportunistic instrument. When making decision for buyback we take into account not only the absolute share price, but also its correspondence with a number of fundamental factors. This being said, the dividends remain our priority, and we understand their importance for shareholders. Therefore, in the current market environment we have taken a decision about the possibility of financing of our buyback with borrowed funds that will let us not affecting the dividends.

Slide 39. High resilience to volatile macro environment

The current market looks very much similar to the first quarter of 2016 – the oil price and exchange rate are roughly the same, and so is a negative tax lag effect. You probably remember that our free cash flow at that time remained positive at about 40 billion rubles.

As usual, our performance is supported by strong vertical integration, largely ruble-denominated costs, progressive tax scale, and high operational and financial flexibility. Furthermore, we have improved our operational performance significantly over the past years.

We have already begun taking necessary measures to adapt effectively to the new conditions.

Slide 40. FCF and EBITDA sensitivity to oil price and RUB/$ exchange rate

Amidst high price volatility, I would like to draw your attention to the fact that LUKOIL's USD-denominated free cash flow is equally sensitive to changes in the oil price or the exchange rate. This is attributable to a large share of ruble-denominated costs, both capital and operating, and does not account for any potential CAPEX optimization that we might perform in an adverse market environment.

Slide 41. Financial position

At present, our balance sheet is very strong. As at the end of the year, total debt stands at 553 billion rubles, while net debt is close to zero.

Low leverage in the current macro environment is a priceless advantage that gives us more flexibility in decision-making.

Thank you. Now I would like to hand over to Pavel Zhdanov.

Pavel Zhdanov

Slide 43. 2020 outlook

Thank you, Alexander. At the end of our presentation today, let me talk briefly about our plans for 2020.

Our base plan suggests hydrocarbon production growth of up to 1% and refining throughput increase of up to 3%. The actual numbers will depend on the market situation.

Our capital expenditures might total up to 550 billion rubles under our base plan excluding the West Qurna-2 project. The plan is based on the 65 rubles per 1 US dollar exchange rate. We will strive to stay within this limit even at weaker ruble owing to optimization of our investment program.

Slide 44. LUKOIL – a unique investment proposition in Oil&Gas

Before we move on to the questions and answers session, I would like to once again highlight the key strengths of LUKOIL investment story.

We combine the best features of both Russian and international oil companies, namely low costs, strict investment discipline, focus on efficiency enhancement, balanced and clear policy for capital distribution, high level of transparency, and strong corporate governance standards.

We benefit from extensive reserves and the quality and sophistication of our refining facilities, and we aim to grow organically with a focus on Russia.

Our key objective is to deliver shareholder value.

In the current complicated market environment our important advantages include the strong financial sustainability owing to the low debt burden and flexible financial policy, as well as the long-term sustainability of our business due to strong vertical integration and focus on Russia with natural hedging mechanisms.

Thank you!