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California Resources Corp. (CRC)

Q4 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon and welcome to the California Resources Corporation Fourth Quarter and Year-End 2017 Earnings Conference Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please also note this event is being recorded.

I would now like to turn the conference call over to Scott Espenshade. Please go ahead.

Scott Espenshade

Vice President-Investor Relations, California Resources Corp.

Thank you. I'm Scott Espenshade, Senior Vice President of Investor Relations. Welcome to California Resources Corporation's fourth quarter and year-end 2017 conference call. Participating on today's call is Todd Stevens, President and Chief Executive Officer of CRC; and Mark Smith, Senior Executive Vice President and Chief Financial Officer, as well as several members of CRC's executive team.

I would like to highlight that we will provide our slides in our Investor Relations section on our website at www.crc.com. These slides provide additional insights into our operations and fourth quarter and year-end results, plus additional information. Also, information reconciling non-GAAP financial measures discussed to their most directly comparable GAAP financial measures is available in the Investor Relations portions of our website and in our earnings release.

Today's conference call contains certain projections and other forward-looking statements within the meanings of federal security laws. These statements are subject to risks and uncertainties that may cause actual results to differ from those expressed or implied in these statements. Additional information on factors that could cause results to differ is available in the company's 10-K, which is being filed later today. We would ask that you review it when available and the cautionary statement in our earnings release.

A replay and a transcript will be made available on our website following today's call and will available for at least 30 days following the call. Please note CRC will also be hosting an Analyst Day on October 3 in New York City. We believe that this will be a great opportunity to get an update on our operations and run you through our strategic plans in detail. And mark your calendar, notice will be sent soon out to you.

As a reminder, we have allotted similar time for earnings and Q&A at the end of our prepared remarks. We'd ask that participants limit their questions to a primary question and a follow-up.

I will now turn the call over to Todd.

Todd A. Stevens

President, Chief Executive Officer & Director, California Resources Corp.

Thank you, Scott, and thank you to everyone for attending CRC's year-end 2017 earnings call. In 2017, we followed the same major tenets of our strategic plan that we have consistently adhered to since the spin. One, we maintained a disciplined approach to developing our world-class assets; two, we focused on projects that offer the best value creation opportunities; and three, we improved our financial position.

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Our plan is clearly working. We lived within cash flow since our inception, a rarity in the E&P sector. Throughout 2017, our banks, investors and joint venture partners repeatedly validated the quality of our extensive inventory and demonstrated confidence in our team.

With the closing of our midstream JV with Ares, we believe CRC is well positioned to create and deliver sustainable value to shareholders in a mid-cycle pricing environment. We will achieve this by continuing to prioritize value-added growth, focusing on factors within our control and further strengthening our financial position.

Our team and our assets continued to deliver throughout 2017. I'm pleased to report that our 2017 development program delivered a strong organic reserve replacement ratio of 119%, as well as single-digit F&D costs of $6.82 per BOE. In fact, this marks the third year in a row that organic F&D costs have been in the single digits and recycle ratios in excess of 2 times. We ended 2017 with 618 million barrels of oil equivalent of proved reserves and 450 million BOE of probable reserves.

Additionally, our proved [ph] SEC-10 (00:04:06) PV-10 value alone increased from $2.8 billion to $4.5 billion. We continue to proactively manage our business through the strategic use of JV capital to enhance the value of our asset portfolio. In 2017, we added two development partners, Benefit Street and Macquarie, in addition into entering into several smaller exploration joint ventures.

These partnerships have allowed us to ramp up overall activity while creating optionality to direct CRC capital to other high-value opportunities. By operating with JV partners, we expect to continue to improve operating efficiencies, maximize capital flexibility and de-risk an even broader inventory of actionable projects just as we did in 2017.

Earlier this month, we announced our third major strategic joint venture, this time with Ares Capital Management (sic) [Ares Management] (00:04:57). We're thrilled to have Ares as a strategic partner investing in our midstream assets, which includes the Elk Hills power plant and gas processing facility. We believe the transaction reflects Ares' strong confidence in CRC and will accomplish two main objectives.

First, it helps validate the value of our midstream assets and, combined with the Ares investment in CRC equity, speaks to the significant long term value creation opportunity ahead. It also aids strengthening our balance sheet. In accordance with our bank agreement, CRC paid off $297 million of outstanding amounts under our revolver.

We intend to deploy the transaction proceeds to the best value alternative, whether that is reinvestment, acquisitions or additional debt reduction to drive long-term shareholder returns. Financial discipline has been our hallmark. CRC's balance sheet has improved meaningfully, reflecting a significant positive change in our credit position. We successfully completed refinancing last November along with executing a bank amendment both of which provide clear runway through 2021 to reinvest in the business above 2017 levels.

While Mark will provide more detail, the important takeaway is that we have received solid third-party validation of the value of our assets, evidenced not only by the refinancing and the bank amendment, but also through the strategic joint venture agreements we have entered into. As part of the due diligence process for these transactions, all of the parties took a comprehensive look into our assets and management expertise.

They voted with their dollars and chose to invest in CRC during a time when capital was rapidly exiting the sector. Their actions and partnership affirm not only our strong development inventory, but did speak to their confidence in CRC. Looking ahead, under our strategic plan for 2018, we will work to further strengthen our financial position

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while continuing to realize the value-driven growth from our world-class assets and drive operational execution to deliver cash margin expansion.

We believe that our recent transactions provide stronger positioning to take advantage of the opportunities before us and significantly increase CRC's optionality to prime the pump to recognize our full value. 2018's operational focus, magnified by CRC's core principles, will enable us to realize even more of that value. From an operational perspective, we continue to profitably and sustainably ramp our drilling activity by utilizing JV capital alongside our internally generated cash flow.

For example, in the Buena Vista Area, the JV provided a lasting value to CRC while providing the capital flexibility for us to advance important resource capture. In this area, partner capital was applied to support our infill program and improve operating efficiencies, while our organic capital is deployed to expand the extent of the play. This was beneficial as we were able to leverage our [ph] geologic (00:07:49) learnings from our known areas to thoughtfully step out and retain all of the upside of the perspective area for CRC.

Our team employed drilling optimization and cost improvement which worked to offset variable performance and preserve attractive project economics. Overall results for this highly perspective area are calculated to achieve a robust VCI of 1.8 on a fully burdened basis at a $55 Brent deck. In addition, success in the greater BV Area contributed an incremental $7 million BOE of proved reserves. These strong operating results exemplify the dynamic nature of our portfolio and demonstrate the benefits we reap from our deep value offering and laser-focused execution.

In addition to our drilling program, we continue to execute our high VCI workovers with organic CRC capital. Across the company, we invested $89 million in workovers that delivered a VCI 2.9 at a $55 Brent price deck.

As we continue to refine our life-of-field plans, we are expanding our inventory of these high-value, low-cost workover opportunities. This year, thanks to our improving balance sheet, we're poised to begin investing above our 2017 capital investment level. Our 2018 capital plan will be deployed primarily on low decline crude oil development and delineation projects in Buena Vista, Kettleman North Dome and Ventura. Some of our largest assets including the greater Elk Hills area, Wilmington, Huntington Beach and Kern Front will see investments focused on new conventional opportunities and expanding waterflood and steamflood projects, along with our capital workovers that have already proven to be highly valuable.

We will begin with a $425 million to $450 million capital program that could potentially ramp through the year as confidence in the current commodity price environment grows. Additionally, we can use our JV capital [ph] flexes (00:09:42) plan as needed, in line with increasing operational cash flows to maintain or grow production over the near term.

Our cash margin performance will also be key focus in 2018. CRC is a large-scale value-focused entity with operating control over nearly half of oil and gas fields in California. Since we have prolific and diverse assets, we can quickly shift our investments between oil and natural gas assets to manage price volatility. Given current pricing, we continue to focus on investment in oil projects. For 2017, crude oil accounted for 64% of our production mix and we expect our oil weighting will grow over time towards the 72% oil mix reflected in our reserves.

The composition of our resource base is a key factor that we believe will aid cash margin expansion along with our ability to grow production and tightly manage production costs. We look to increase efficiencies, reduce

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controllable costs and optimize our integrated infrastructure in 2018 to extract even more value from new and existing production.

Our commitment to operational excellence remains a high priority across our organization in 2018, while sustaining our strong safety and environmental performance. CRC continues to help California address its pressing energy, economic and environmental goals. We have served as the net water supplier to agricultural water districts every year since our formation. In 2017, we again set a company record treating and delivering 4.9 billion gallons of reclaimed water for agricultural reuse. CRC's team also won four national safety achievement awards in 2017 from the National Safety Council. As a responsible partner of choice within the state, we proactively engage with regulatory agencies, community leaders, labor groups and other stakeholders to purse mutually beneficial outcomes, and expand opportunities for the communities in which we live and work.

We've been able to achieve this level of operational excellence thanks in no small part to Bob Barnes. As you may have heard, we started the year with the leadership changes at CRC as part of the company's succession planning. As Bob eyes retirement, he will move into an advisory role to continue shaping CRC's future as he mentors many in our organization with his vast experience, knowledge and camaraderie. I'd like to thank Bob for his 40 years of commitment to CRC and its predecessor companies. His expertise and judgment helped CRC navigate the commodity price downturn while getting the most out of our asset base.

At CRC, we're constantly focused on adapting our business model to best generate shareholder value given market dynamics. Our business opportunities dictate our structure, not the other way around. To lead the team's operational growth moving forward, Shawn Kerns and Darren Williams will focus on production and margin growth as well as resource capture.

To help this effort, we recently took steps to align our organization in a way that maximizes the value of our assets from a cash margin and VCI perspective, while ensuring that teams are working collaboratively, live safely and creatively to achieve operational goals.

In summary, with our strategic plan in place, CRC is rooted in creating and delivering sustainable value to shareholders while maintaining our commitment to invest within cash flow and prioritize value-driven growth in 2018 and beyond.

Now I'd like to turn the call over to Mark.

Marshall D. Smith

Chief Financial Officer & Senior Executive Vice President, California Resources Corp.

Thanks, Todd. I'm proud of what we've achieved. We've taken several steps to create a substantial runway for the future. With a stronger balance sheet, we're now positioned to capture significant operating leverage as the crude market continues to strengthen and we work to deliver value-driven growth from our operations.

Our stronger financial position results from several actions we executed in the fourth quarter of 2017 and early 2018. In November, we worked to secure an amendment and complete financing that created additional financial flexibility and improved our liquidity. We repaid the outstanding balance on our 2014 Term Loan facility and subsequently repurchased a portion of our senior notes to eliminate the related springing maturity provisions in our credit agreement.

More recently, we announced our strategic partnership with an affiliate of Ares for our midstream assets, including the Elk Hills power plant and gas processing facility. As a result of that transaction, we were able to repay debt

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more quickly and also provide more capital for operations or other value-enhancing opportunities. We have significantly more optionality and improved positioning to take advantage of the strong opportunities before us. With a bolstered cash position and increased financial flexibility, we now have significant liquidity and nearly four years of runway providing us with the wherewithal to build momentum through 2018 and beyond.

In terms of shrinking our balance sheet going forward, I tend to think about our leverage in terms of debt to EBITDAX. We're focused on both reducing the numerator as well as increasing the denominator. We'll also continue to work to reduce our fixed charges and simplify our balance sheet over time. We believe we'll be able to accomplish this, as Todd said, by allocating capital to the best value alternatives, whether that's investment to grow our business or to reduce debt.

In our earnings slide deck, we've presented an indifference curve to provide insight into one of the ways we think about these different opportunities using our disciplined investment approach. The curve plots our VCI metric on the y-axis and bond discounts on the x-axis. Recall that for a project to receive investment at CRC is VCI must be greater than 1.3. If we have resource returns on investments greater than our indifference curve, we believe we're better off investing the money in the ground versus buying back debt in the open markets.

Our planning scenarios show that current or higher oil prices we can strengthen our financial position more effectively by redeploying our cash flows into operations and by paying down debt. However, this is not a standalone exercise. We'll continue to evaluate each alternative's underlying value proposition with a firm commitment to continue to de-lever. We'll do this by reducing debt in absolute terms as we've done in the past by continuing to grow our EBITDAX or by some combination of both.

A look back at our 2017 capital program shows a potential of our asset base to de-lever organically and drive value for CRC shareholders over the long term. At a $55 flat Brent price deck, our development program had a 1.7 VCI on fully burdened investments.

[ph] We don't have (00:16:10) cycle costs or cherry-picked wells. This analysis includes both good wells and bad wells and associated infrastructure for those particular projects. Applying a $65 Brent price deck from 2018 forward, we'd achieve a 2.0 VCI, as shown on our slide deck. For reference, we've included fully burdened IRRs on the slide as well. We understand that reinvestment in drilling and workovers carries execution risk not found in repurchasing bonds. By utilizing fully burdened VCI calculations for actual 2017 program, we seek to provide a forthright look at our potential opportunities. These risk results are well above our cost of capital we expect will create real value for shareholders and we continue to increase our capital plans to align with commodity prices.

Now turning to our financial performance for the fourth quarter and full year 2017, I'm pleased to report that we delivered results within our stated guidance range. We produced an average of 126,000 BOE per day in the fourth quarter. This result reflected our gradual increase in activity during the second half of 2017. The increased activity partially offset the impact of significantly reduced investment through 2016. Our results also include approximately 1,300 BOE per day of negative PSC effects due to higher realized prices compared to those at the time of our guidance as well as a 700 BOE per day impact for the quarter due to California wildfires that occurred in December.

We expect similar effects to continue in the first quarter. Our first quarter guidance incorporates approximately 1,200 BOE per day negative impact in January or 400 BOE per day for the quarter due to third-party power issues from the fires and mudslides, a 600 BOE per day impact for PSC effects, as well as results from a significant well that did not meet timing and performance expectations.

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While the rise in oil prices were strong during the fourth quarter, the effects on our income statement were tempered due to our hedging contracts which were first put in place when prices were much lower. However, we continue to benefit from premium Brent-based pricing realizations. Oil differentials were healthy registering a strong 97% of Brent and 92% including hedges.

NGL realizations also remained healthy reflecting tighter domestic supply and the strength in the exports. We anticipate these dynamics to continue in 2018. Natural gas realizations continue to see seasonality trends which will magnify due to limited third-party storage within California. Production costs for the fourth quarter of 2017 were $227 million or $19.64 per BOE, within our stated guidance range. The year-over-year increase was driven by increased activity in line with stronger commodity prices and higher gas and electricity costs.

Adjusted general and administrative expenses were $5.80 per BOE, which were higher than guided as a result of the higher costs for performance-based bonus and incentive compensation plans due to increases in share price. Excluding these effects, adjusted G&A for the quarter would have been $5.44 per BOE.

For the fourth quarter, we reported a net loss of $138 million attributable to our common stock or $3.23 per diluted share. Adjusting for unusual and infrequent items such as non-cash derivative losses that are generally excluded from core earnings by investment analysts, our net loss would have been $14 million or $0.33 per diluted share.

Adjusted EBITDAX for the fourth quarter was $222 million, up 32% from the prior year period, reflecting margin expansion from 34% to 39%. CRC reported cash flow from operating activities of $23 million in the fourth quarter and was free cash flow neutral for the full year, excluding $96 million of the capital funded by BSP. Our results demonstrate the capital discipline that we continue to apply throughout our business.

As Todd noted, our proved reserve position of 618 million BOE, our enhanced life-of-field development plans and better than expected well performance allowed us to replace 119% of our production, excluding the effect of price adjustments. Despite a limited 2017 capital program, we added 34 million BOE of proved reserves from extensions and discoveries and 22 million BOE from performance. We were also able to rebook 49 million BOE due to the increase in prices compared to 2016.

Organic F&D costs including price-related revisions were $6.82 per BOE in 2017 and produced a recycle ratio of 2.1 times. This is the third year in a row that our organic F&D costs have been in the single digits averaging $4.80 over this timeframe.

Additionally, we've grown our probable and possible reserves by 302 million barrels, a 37% increase from the prior year. These additional reserves provided a ready source of projects as our cash flow increases at about current prices and will provide ample opportunity to accelerate further developments using our cash flow supplemented by our JVs. Our slides also show the price impact on our reserves since the spin. We would expect approximately a quarter of those to come back at $65 Brent.

Turning to 2018, our capital budget for this year is planned between $425 million to $450 million. This includes approximately $100 million to $150 million of JV capital and represents a slight increase for internally funded CRC capital [ph] reporting (00:21:41) 2017 levels as we transition to a mid-cycle pricing environment.

Our 2018 plans assumes Brent and NYMEX natural gas at about recent levels based on strip pricing. As we've stated before, we have dynamic plans and we'll strategically use levers such as JV capital remain within cash flow as well as prudently ramp activity.

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Please note our current 2018 capital plan does not reflect the use of proceeds from the JV transaction with Ares. To protect against our spending cash flow due to downdrafts in crude oil prices, our hedge program currently covers a significant portion of our oil production for full year 2018 as detailed in our earnings release. Our philosophy regarding hedging continues to target up to 50% of our production in order to provide more certainty in cash flows and underpin our capital program. Please refer to our earnings release for the details on our hedging positions and counterparty options.

We strengthened our financial position and continue to align our organization for the commodity environment at hand. Our assets are responding and, with the support of our strategic JV partners, we're poised to increase activity, grow cash flow and maximize value creation.

Please note that we provide a detailed analysis of adjusted items as well as key first quarter 2018 guidance information in the attachments to our earnings release. I'll be happy to take any questions you may have on that information and other aspects of our results during the Q&A portion of this call.

Thanks and I'll now turn it back over to Todd.

Todd A. Stevens

President, Chief Executive Officer & Director, California Resources Corp.

Thanks, Mark. We're poised to build on the solid foundation we established in 2017. As we prudently ramp capital investments to a sustainable level in line with available capital from cash flow and JV partners, we will allocate capital to the best value alternative. With our high level of optionality, we will do as we have always done and flex activity to meet our disciplined investment criteria.

Our resilient assets have a low base decline and low capital intensity that benefits us throughout the commodity cycle. Importantly, CRC's management team has decades of experience operating these assets, with a strong track record of driving down controllable costs and increasing efficiencies. Each time we improve margins, more of our inventory achieves our ambitious VCI hurdle.

We're excited for 2018 as we look to benefit from the current commodity price environment and continue to build on strong momentum throughout CRC's operations. Our focus will be centered on showcasing CRC's world-class assets, driving exceptional operational execution with character, responsibility and commitment, and further strengthening our financial position to deliver value for our partners and investors.

We now welcome your questions.

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QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] At this time, we will pause momentarily to assemble our roster. The first question comes from Doug Leggate with Bank of America Merrill Lynch. Please go ahead.

Doug Leggate
Analyst, Bank of America Merrill Lynch

Q

Thanks. Good afternoon, everybody. Thanks for taking my questions. Todd or Mark, whichever one of you guys wants to take this, I mean, when you look at the 2019, looking at slide 17, there seems to be a fairly substantial step-up in your capital plan. Is that – what's the basis of that? Is that living within cash flow or was it using some of the proceeds that you've put on the balance sheet or what is your thought process on that step-up in spending as you go into 2019?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Oh, that's – okay, Doug, this is Todd. On the scenario we're portraying there, that's one scenario where we talk about production growth and EBITDAX growth, you've seen the chart from us before, and this is the capital that goes along with that. That doesn't mean anything more than that's one scenario that could play out if not a kind of foreshadowing or giving guidance on a business plan for 2019.

Doug Leggate
Analyst, Bank of America Merrill Lynch

Q

So, as things stand today, the plan is still to live within operating cash flow or to use cash on the balance sheet?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

At this point in time, we would plan to use operating cash flow, but we might supplement that with other cash flow if the opportunity from a value perspective merits it.

Doug Leggate
Analyst, Bank of America Merrill Lynch

Q

Okay I appreciate that. My follow-up is also [ph] kind of a longer depth (00:26:13) question. When you go back to the very beginning of the company as a standalone entity, Todd, you used to talk about you'd be dead before you got a chance to drill all the drilling locations that you had, but you didn't want to monetize into a fire sale type situation. Well, we're not really in a fire sale situation anymore and I don't really think you've done – you've done some innovative things for sure, but not as it relates to the very longer-dated drilling inventory. So what are your thoughts in terms of additional monetizations? And I guess I've got one final one if I can squeeze it in after that.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Sure. I think it's twofold. I know from day one of the spin back there in October, it was at Halloween of 2014, we talked from day one we needed to bring down our absolute debt level, we understood that. We looked at

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monetizing different ways the midstream assets, and you saw us finally do that in a way that we feel like it's most advantageous to ourselves and with our – with a great partner.

On the upstream side, along the way here, we have monetized some small amounts of assets along the way. We got to remember, everything we have under our portfolio, we're doing life-of-field plans and it has to compete for capital. If it's not competing for capital or it's too long dated in the current environment, we're going to look to use joint venture dollars or ultimately sell it. So I think for the right price, really, everything here is on the table from an external standpoint.

But, yeah, I think, you're right, the environment's changed. I think we've underpinned a different commodity price environment. So we would look to do that if they've made sense that we weren't going to get to things like we talked about that in my lifetime or in the short or the amount of time that would take for us to, either internally or with joint ventures, to invest in that kind of assets.

Doug Leggate Q
Analyst, Bank of America Merrill Lynch

So nothing on the table for now or should we expect to see that change in 2018?

Todd A. Stevens A
President, Chief Executive Officer & Director, California Resources Corp.

We have had active discussions with numerous folks along the way here during the fire sale portion, that was occurring for some time, but I think we have ongoing discussions both on the joint venture partners and with the potential sale of certain assets that just don't compete for capital. And I think the one thing [ph] that's lastly (00:28:24) we didn't highlight quite so much, we hinted at it, was at the year-end, we had six exploration wells being drilled with other people's money. So I think that's important to understand that we [ph] did execute (00:28:35) on a lot of small joint ventures that are really value additive, and this is real [ph] well cutting, this isn't (00:28:41) stepping out two locations from a [ph] PUD (00:28:43).

Doug Leggate Q
Analyst, Bank of America Merrill Lynch

All right. Thanks, guys. I'll leave it there. Thank you.

Todd A. Stevens A
President, Chief Executive Officer & Director, California Resources Corp.

Thanks, Doug.

Operator: The next question comes from Brian Singer with Goldman Sachs. Please go ahead.

Brian Singer Q
Analyst, Goldman Sachs & Co. LLC

Thank you. Good afternoon

Todd A. Stevens A
President, Chief Executive Officer & Director, California Resources Corp.

Hey, Brian.

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Brian Singer
Analyst, Goldman Sachs & Co. LLC

Q

You reiterated in the press release just the response times and the production profiles on steamfloods and waterfloods. Naturally, they take a little bit more time to provide the uplift. Can you just give us your latest expectations here and how the wells that are showing uplift or mitigated declines are performing relative to expectations?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

I think our overall corporate base decline hasn't changed. It's probably mitigated a little further, as we've talked about, kind of very low single digits. And we have parts that clearly that can be lower than that. I think if we talked about individual type drive mechanism, I think there's – not a lot has changed overall [ph] or from (00:29:42) the company perspective. I think we – when we looked at it and we talked about the Buena Vista wells and the performance there, those are all wells that we – are pretty heavy hitting good wells, good – as you saw we – incremental 7 million barrels of proved reserves and that we haven't finished the program there yet. So I think, overall as a company, the portfolio effect works well for us and we still have a very low single digit – I mean, double-digit base decline for the company.

Brian Singer
Analyst, Goldman Sachs & Co. LLC

Q

Great, thanks. And then with regards to the quarterly projection trajectory, can you give us a little bit more color on how this looks through the year? In the fourth quarter, production had fallen sequentially. Fourth quarter of last year, you highlighted some of the one-off reasons for that, the wildfires, the PSC impacts. Can you just talk a little bit more about the more same-store sales momentum and whether you're in on a more gross [ph] basis and growth mode (00:30:42) flat or still declining?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

When we look at coming into fourth quarter and the year – and where we started the year, clearly, not the way you want to start the year with the mudslide and the fires that occurred. And we had obviously an impact on the company. The positive impact that occurs from a net production perspective is the PSC effect, because that means we're getting higher prices. So that occurs but that's something you can't really plan around [ph] you, just hope you get (00:31:10) lower production [ph] from their prices. (00:31:09)

And we did have one well that we ended up having to sidetrack the expectations and the timing, it turned out to be an okay well in the end, but the timing didn't come in the fourth quarter. Some of that hangover from the fourth quarter particularly on the mudslides and the fires carried into January. There is a very, very tiny amount of production still impacted now, but it's more about economics and third-party issues that we're dealing with on this amount of production.

So, the vast majority of what was down is up. So when you look at the trajectory, I think, clearly, we had a rough January because of that. But I think the rest of the quarter is looking more positive, and I think you'll see us bounce back to more of a trajectory [ph] like (00:31:54) in the second quarter that looks flattish to maybe moving up a little bit depending on performance through the quarter.

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Brian Singer
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thank you very much.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Thanks, Brian.

Operator: The next question comes from James Spicer with Wells Fargo. Please go ahead.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

Hi. Good afternoon.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Hi, James.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

I'm wondering if you can just talk a little bit about how much of your total production is coming from joint ventures at this point and talk a little bit about the pace of incremental capital coming in throughout the year in 2018?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

So we can't really talk about where it comes from because, remember, the two joint ventures currently [ph] – well, I won't (00:32:37) talk about the exploration joint ventures. The two upstream development joint ventures, BSP, remember, that's a little bit different, that's not a traditional joint venture. And then on the Macquarie side, that will be about 10%, [ph] remember, (00:32:52) of their investment of their production until payout comes to us.

And so, the BSP, we're going to get it maturely most of the production from the joint venture. And so – but I don't think we disclosed that at this point in time. I think it's currently all we can really say is it's less than 2,000 – probably somewhere between 1,500 and 2,000 BOE a day.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

Okay. Okay. No, that's helpful. And then in terms of the pace of capital coming in throughout 2018?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. So, remember, it's in tranches. The BSP joint venture is in $50 million tranches, and we're still in the first tranche, first $160 million tranche of Macquarie. So that pace will continue through the year. I think you'll see us probably draw down one more tranche from BSP as we go through the year. But I think when you look at our earnings release, you'll see we've given a little bit of guidance around where we think that'll be at this point in time, plus or minus $100 million is probably a fair number.

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James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

Okay, thanks. And then for my follow-up here just on the CapEx side, can you just talk a little bit about the – obviously, you're sitting on a lot of cash now post the Ares transaction. Can you talk a little bit about the priorities in terms of capital allocation there and whether you think you may be able to supplement that with free cash flow generation in 2018?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yes. So I think it's – we have these proceeds, gives us an exceptional amount of flexibility and optionality as a company. But for us, having cash in the bank is not what we want. We want to actually invest or utilize that to create real value for our shareholders. So when we look at it, I think the priorities, as I outlined in my remarks, were really looking at putting it in the ground in some way. When I say some way, I could mean, could we do an acquisition that made sense for us, that was accretive from both an operational and financial perspective or could we put it in the ground in a way that creates value using our VCI and other metrics from an inventory standpoint or, as Mark alluded to, [ph] look at (00:35:28) buy back our debt.

We have that indifference curve we've outlined where we talk about where our debt trades, and really, we focus on the seconds at this point in time. And they have to meet a minimum threshold discount for us to be able to purchase them, but looking at that and making sure that it's something that creates real value for us. Also understanding that that, when we purchase debt, clearly, there's no execution risk with the exception of finding a willing seller as it is with executing on filling inventory or buying something.

So, again, we will compensate ourselves from a higher VCI perspective if we were going to execute on the inventory or purchasing something that really had to be well in excess of the value perspective we would get from buying in debt. Because I think people have to understand that that overarching concept here is we do want to bring down the absolute amount of debt, but there's no one single way we're going to do it. We're going to do it kind of an all above strategy with growing our EBITDA, chipping away at the debt, whether it's buying it in at a discount or other creative methods, as we've shown along the way.

So I think, from that perspective, that is – when you look at kind of the use of proceeds, that's how we're looking at it. And we're not going to sit here and wait forever, we're going to turn around and utilize something to create real value for our shareholders here in the near term.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

Okay. All right, Todd, thanks. Thanks very much.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Thanks, James.

Operator: The next question comes from Pavel Molchanov with Raymond James. Please go ahead.

Pavel S. Molchanov
Analyst, Raymond James & Associates, Inc.

Q

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Thanks for taking the question, guys. So, your capital program is going to be at a three-year high and I suppose the – I go back to some of the commentary you had made back in 2014, 2015 about the drilling permit bottlenecks that had, in those days, been impeding some of your activity. And I would just pose the question, to what extent could that become a hurdle now that you're back at half of the peak rig count that you had in those days?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. Pavel, we don't see it being an issue for us. We keep very close track of our days of drilling inventory, from a permit standpoint, I think we're at record highs for the company, we continue to grow that. Our goal is to get out there a year, but I mean, we're not close to that at this point in time, but we're doing fairly well for ourselves. Could there be one-off issues with particular permits in certain areas? Yes, and there could be some delays, but that's what great about having a portfolio like we have where we can displace that with another great project if necessary.

And so, we – there is a lot of planning that goes into, as you know, our life-of-field plans in our portfolio. So, again, having a very sophisticated process enables us to have alternative projects in case of that. We've planned for that in some cases and we also, as I've said many times, here the [ph] Gantt chart (00:38:46) on certain projects is just going to be long because you have to get through the permitting processes of California in certain areas and typically if it's a more greenfield project. So from our perspective, we've planned for that and we feel like we have a very good handle on it, and the level of detail and the people working on it, I feel better – much better now than I did in 2014 for sure.

Pavel S. Molchanov
Analyst, Raymond James & Associates, Inc.

Q

Okay. And then sort of along those lines, there are, at least anecdotally, reports of more and more cities and county governments that are imposing various kinds of drilling restrictions above and beyond what the state directly may be involved in. Have any of those been impactful at all to your operations or is it really just a PR move by those cities?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

I think in some cases, these cities, counties, whatever local government you're talking about, in some cases, are put up to these things by activists. And what happens is it's a publicity stunt, a fund raising stunt in some cases and in some cases, it's serious. You saw what happened in Measure Z in Monterey County was struck down in court. We weren't involved there. We had some – we didn't have production, but we had minerals that [ph] we've considered taking (00:40:10) from a legal perspective. I think that sets a precedent for people that want to dabble in this from a local government perspective.

So, other than that, I do think that we make a concerted effort to work with the communities we live and work in and establish what we do, what we don't do, the benefits we bring to the communities we live and work in. So I don't think it's been much of an issue at all where we have operation. But we do work very diligently on this with our partners and the community and with the labor and everyone else to make sure people understand what it is we do and don't do, because a lot of these initiatives are very misleading. And they mislead the voters and mislead the people they represent.

Pavel S. Molchanov
Analyst, Raymond James & Associates, Inc.

Q

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Great, appreciate it, guys.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Thanks, Pavel

Operator: The next question comes from Jason Gilbert with Goldman Sachs. Please go ahead.

Jason A. Gilbert
Analyst, Goldman Sachs & Co. LLC
Q

Hi, guys, thanks. Most of mine have been answered, but I did want to follow up on F&D costs. You put up, I think for the third year in a row, pretty low F&D costs. And you're below your DD&A per barrel. How do we – and below peers also in California. How do we think about the right F&D cost going forward? And specifically, are there certain low-cost activities that you're doing now that are maybe finite in nature that may run off at some point?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

I think if you look at, you're right, the DD&A rate is a historical [ph] lighting (00:41:42) indicator of F&D. I think that's going to trend down over time. And I think when you look at our portfolio and our reserves, you'll see our F&D, in my mind, when I go through and calculate the total portfolio, it's sort of $7 to $10, $7 to $9 range over time. So I think, if you use $10 plus or minus or $9 plus or minus, I think you would be there. But I would [ph] try into (00:42:10) this point and think that, over time, it's probably going to come down from there because – as we continue to get better and find the projects we have and have more exploration successes...

Jason A. Gilbert
Analyst, Goldman Sachs & Co. LLC
Q

Okay.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

...which is great for your F&D.

Jason A. Gilbert
Analyst, Goldman Sachs & Co. LLC
Q

Great. Thank you. And [indiscernible] (00:42:25) to follow up, which is the housekeeping item. Cash flow in the quarter looked a little lighter than we had expected. Was there a working capital use in the fourth quarter?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Yeah. And remember, in November, we pay property taxes in California. That's the – you pay them in April and November, you pay the – that's the way [indiscernible] 00:42:47) is the way you really – the way the fiscal regime works and it was a – also, as you start ramping activity, you have the issue with how account payable and receivables work. But, yeah, I think it was about a $50 million plus or minus working capital adjustment in the quarter.

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Jason A. Gilbert
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thanks. I'll turn it back.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Thanks, Jason.

Operator: The next question comes from Sean Sneeden with Guggenheim. Please go ahead.

Sean M. Sneeden
Analyst, Guggenheim Securities LLC

Q

Hi. Thank you for taking the questions. Maybe just on the LOE guidance, could you talk about that just being sequentially higher? Is that driven by the midstream deal or is that due to the fire and mudslide impact on that as well or any kind of thoughts around how we should really think about kind of normalized LOE going forward?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. I'd tell you how I look at it because when you have these one-off impacts or the PSC impacts that really could affect that either way, it's really – the focus is on the absolute dollars being invested and spent here on operating cost. So, a little bit of that is PSC effects, a little bit of that is coming into the year a little rough and the volume being down a little. But I think, overall, our plan keeps us for the year that the production costs are going to be kind of flat for the year, if not down overall. And that's really what our focus is on an absolute basis.

As we grow out of this hiccup here at year-end 2017 coming into 2018 from the fires and mudslides, I think you'll see us raising production to the extent we can from a gross basis. But obviously, and that could be affected by the PSC, but that's really my focus is really looking at the absolute costs. And we do give you a little bit of guidance in there about how the PSC could affect production at different price levels.

Sean M. Sneeden
Analyst, Guggenheim Securities LLC

Q

Sure. No, that's helpful. And just to kind of make sure I understand it, for the full year, you're thinking that absolute dollar should be kind of lower on the LOE side and perhaps, without the PSC effects, maybe you'll see that on the unit side as well. Is that right kind of [indiscernible] (00:45:06)?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Correct. I think it will be about – absolutely will be about flat to down and on an absolute basis for the year, and that's what we're targeting. And that's we're working on right now. On – obviously, the PSC effects could move it around and you should see us flattening to growing production as we come out of this hiccup coming into the year.

Sean M. Sneeden
Analyst, Guggenheim Securities LLC

Q

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Okay. That makes sense. I guess, I think you had mentioned, Todd, that we should start getting back to kind of normalized production levels by around Q2 and then, I mean, we should think about that quarter kind of being flat to maybe modestly up. Was that comment geared around flat to modestly up versus the first quarter guidance or is it versus like a more normalized level that you were talking about?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yes. It's more normalized level. If you took out what happened at year-end and start of this year, it was [ph] assuming it didn't (00:46:00) happen, that would be our goal is where we would be.

Sean M. Sneeden
Analyst, Guggenheim Securities LLC

Q

Okay. And that's kind of more or closer to like 130,000 a day type of number, is that how we should think about it?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

We haven't provided that. But if you looked at year-end, you looked at like the 3Q, where we were at in 4Q, where we were at before the fire impact which was about 400 BOE a day, fire and mudslide in – for the quarter, it was higher obviously in the month of December, I think then that would be more what we would think we'd be at.

Sean M. Sneeden
Analyst, Guggenheim Securities LLC

Q

Okay. That's helpful. Thank you very much.

Operator: The next question comes from Jacob Gomolinski-Ekel with Morgan Stanley. Please go ahead.

Jacob Gomolinski-Ekel
Vice President, Morgan Stanley

Q

Hey. Thanks for taking the questions and congratulations on the recent transactions and Bob on the retirement. Just given the – on the JV side with the power plant given you got $750 million in the door in kind of if we assume CRC is the only customer for that, should we assume that your costs will go up by, call it, $71 million a year to fund the cash portion of that preferred dividend and eventually $101 million after two years once the preferred [ph] stops peaking (00:47:14)? And I guess I think that translates to about $1.50 to $2 a barrel using the 130,000 BOE or 120,000 BOE a day of production?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. Remember, it's a preferred interest. It's not OpEx. And I think you got it approximately right. But also remember, as the – power plant is something that we constantly try to utilize the power generated there in our operations because it's cheaper than we could purchase it from the grid. So we continue to expand its uses internally, around 35% of the power currently is used internally, continue to look to grow or even grow our customer base even outside of CRC so that we could have this be more beneficial to us and to the bottom line to our partners and Ares.

You got to remember, this is something, when you look back, like I mentioned to Doug, from day one, we are looking at a way to bring down debt and monetize these in a way that would be mutually beneficial. We weren't

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really interested just monetizing it to someone and trading balance sheet leverage or income statement leverage. This is truly a partnership and something that takes into account the important operational aspects of the plant for our benefit. And it gives us a strategic partner that's not only is invested in our power plant but are in our equity.

So I think it's important to understand that this is a real partnership and not just some kind of classic just business transaction that we're over and done with and move on down the road. So, we're excited about it. It's something we've been working on for some time. Clearly, there are some other priorities given what happened between the spin and now. But we feel this is the right time to start bringing this down and be able to utilize the proceeds to create a lot of flexibility and optionality for us to invest in the business or to buy in debt if it trades at the right discount.

Jacob Gomolinski-Ekel
Vice President, Morgan Stanley
Q

Got you. And I appreciate the fact that you'll maintain operational decision-making out there, I guess, I just want to make if I'm understanding this correctly. So when you say it won't be an OpEx item because it's preferred in a JV that you own, how do you do – so is that not taken into account then, like, will those cash flows then be sort of in a financing section and not taken into account...

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Yeah. I'll give it to Mark and Mark can explain where it'd be in the balance sheet and then the income statement.

Marshall D. Smith
Chief Financial Officer & Senior Executive Vice President, California Resources Corp.
A

Yeah. Let me try to add some clarity here. From – in terms of geography on the balance sheet will reside between debt and equity, and on the income statement, it will come through – those dividend payments will come through the line item that's already there. That's described as net income attributable to non-controlling interest. So that's why it won't run through the operating expense that we used to see, and it will run through the cash flow statement as a financing.

Jacob Gomolinski-Ekel
Vice President, Morgan Stanley
Q

Got it. Okay.

Marshall D. Smith
Chief Financial Officer & Senior Executive Vice President, California Resources Corp.
A

Okay. [indiscernible] (00:50:07)

Jacob Gomolinski-Ekel
Vice President, Morgan Stanley
Q

And then maybe just how to think about it bigger picture on the JV [ph] because (00:50:13) I appreciate that it's a partnership. Is the right way to think about it maybe from a more traditional or more simplistic valuation approach that you basically lease the plant for 10.5 times cash flow or 7.4 times total or, like, maybe said differently, like, given the preferred [ph] of the JV boxes (00:50:34) ahead of your equity, is it – I mean, I guess, you could kind of talk of – think of it is like 13.5% or 9.5%, [ph] whether you just pick your (00:50:43) cash financing on those assets?

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Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

I mean, you can characterize it however you see fit it. I'm sure different holders in the capital stack, whether they'd be equity or debt, will choose their characterizations how they see fit. But I think from our perspective, we're excited about it. It's – we view it as a valuable investment, a valuable partner and we think the partnership will grow over time.

Jacob Gomolinski-Ekel
Vice President, Morgan Stanley

Q

Yeah. No. I mean, [ph] it's de-levering in the way, (00:51:11) I just was trying to make sure I'm not thinking about it the wrong way, [ph] though. (00:51:16) Maybe just last question from me. The NGL pricing looked very strong again this quarter. Can you talk about what's driving that and maybe if you see that as continuing going forward?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. I think you got to remember if you step back a 50,000-foot level, California has a very big energy deficit, in imports, two-thirds of its oil from outside the state, 90% of its natural gas and from an NGL basis, it's also an island. So we don't – we always get a premium to Mont Belvieu. We're not tied into the kind of NGL infrastructure that's there in the Gulf Coast. So you'll see us have strong realizations. The primary markets are in Mexico and Canada for us. And we did have a little bit of a tail-off [ph] over (00:52:10) a little bit there, but I think we're kind of back to normal and very strong realizations on our NGLs, which if you look at historically it's been that way.

Operator: The next question comes from Gregg Brody with Bank of America Merrill Lynch. Please go ahead.

Gregg Brody
Analyst, Bank of America Merrill Lynch

Q

Good afternoon, guys. Just a couple for you. The first one, so the midstream JV, could you talk about what the opportunities set for you to grow that business in terms of organic opportunities and M&A, how are you thinking about it?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

So, obviously, we have our portfolio that we can use the proceeds, invest in our portfolio of inventory, or you look at the assets that could potentially be for sale in the company whether – I'm sorry, in California or elsewhere. We're not – we do have an AMI that goes back to the spin, but I think that we could use the proceeds if it made sense. I don't think most things in North America compete with California when we look at it from a value perspective especially when you talk about M&A deals. But we have a competitive advantage from an operational standpoint, from infrastructure standpoint and really anything that could be for sale. And there's been some things that had a high level of turnover, whether it be bankruptcy or other things where assets are being held in California by folks that might not be long-term hands.

So that's something we have to balance it off. But obviously, from my perspective, the cash is burning a hole in my pocket, so I want to make sure we utilize that instead of getting the miniscule interest we get. We can go out and invest in something that's going to create real value for our shareholders, whether it being in the ground, through an acquisition or in the ground through inventory or buying back debt at a discount. And that's really what we're looking at really hard right now and losing sleep at night about.

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Gregg Brody

Analyst, Bank of America Merrill Lynch

Q

And maybe I – I'm sorry maybe I didn't ask my question clearly. So, I appreciate all that and I think I didn't mean to make you repeat that. My question was specifically about the midstream – in the midstream power plant JV, I'm trying to see how you see creating value at that entity. And where I'm going with that is, how much can you potentially grow the volumes there yourself, how much can you do it outside of the CRC system by bringing in other E&P assets, other volumes? And ultimately, how does that lead to – I recognize there are more structure here that allows for an eventual sale of this asset five to seven years from now, who knows, maybe sooner. But trying to figure out how you're thinking about the value creation there [indiscernible] (00:54:58).

Todd A. Stevens

President, Chief Executive Officer & Director, California Resources Corp.

A

Okay. Sorry, Gregg. Sorry, I went down the other rabbit hole. But from – what we've done and we've been very successful, you got to remember the power here is generated at the small percentage of the cost of where we pay for power in the grid. So connecting new fields or connecting our existing fields that are nearby is enviable for us because we're in a power-intensive business. So I think that's very important. But also, we can connect our other midstream assets or other people's midstream assets or we can bring other people's volumes who might be – who have an older outdated plant that doesn't have good a technology or has some requirements from a capital standpoint to meet new AQMD standards or something like that.

So, I think there's a lot of potential synergies here in addition to the complex of assets that exist around Elk Hills. I mean, if you look at within a 10-mile radius of Elk Hills, I think there's three multi-billion barrel oil fields and a lot of smaller oil fields that could be tied in in some fashion that has the best stamp from the standpoint of gas processing facility West of the Rockies, the most sophisticated, and then also our power plant which we can internally generate the power or sell it to somebody at a discount, but still make a profit for ourself.

Gregg Brody

Analyst, Bank of America Merrill Lynch

Q

So, if you think down the road, I mean, I recognize there's [ph] much (00:56:21) provisions in there to allow for an [ph] exit pipe or areas (00:56:24) with the sale and IPO. How do you think this JV is going to exit its current financing structure and ultimately potentially monetize more value?

Todd A. Stevens

President, Chief Executive Officer & Director, California Resources Corp.

A

I don't know if I could see five to seven years into the future, but I think at this point in time, I mean, some of those provisions were put in for different reasons other than what a traditional partnership would have. It's more driven by tax or other considerations. But I think, at this point in time, we do it as a real partnership. And as we get closer to [ph] those three (00:56:59) decision points for ourselves, we'll have to take that into account at that point in time. But I think at this time, we're just very bullish about it looking to grow the business that we're involved in here from both a volume perspective and tying in more existing assets whether they'd be ours or someone else's that could benefit both parties. So, yeah, it's hard for me to say what will happen in five, seven years from now.

Gregg Brody

Analyst, Bank of America Merrill Lynch

Q

Got it. I was just wondering if you were thinking about an IPO in the near term or medium term, but I [indiscernible] (00:57:29)...

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Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Well, we can think of everything. I mean, there's not a thing we haven't thought about. So we've looked at should we do some of this on our own, should we create our own MLP, should we work with other folks. I mean, there isn't I think an opportunity we haven't bedded, but we really feel like we hit the sweet spot here with our partnership with Ares.

Gregg Brody
Analyst, Bank of America Merrill Lynch
Q

I appreciate the time, guys. Thank you.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Thanks, Gregg.

Operator: The next question comes from Joseph Von Meister with Bennett Management. Please go ahead.

Joseph Von Meister
Analyst, Bennett Management Corp.
Q

Hi, guys. This is hopefully a quick one. The Q4 guide was for Q1 production of 120 MBOE to 125 MBOE. The Q3 guide was 125 MBOE to 130 MBOE and the Q2 guide for Q3 was 127 MBOE to 132 MBOE. So, in the midst of putting some significant capital to work, production guides have been coming down. I wonder if you could bridge me to what you guys think is normal.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Well, so when we were coming at – going to last year or through last year, we talked about we reached this inflection point. And I think the hiccups on the fires, mudslides, and we talked about one particular well also that has enabled us not to kind of bottom out or flatten out at the bottom where we wanted to. I think clearly we probably have at this point bottomed out when we look at everything and we're continuing to focus on investing from a standpoint of – from a maintenance capital standpoint as we've always talked about and start to flatten out. And the decision then comes into play here as we come into this year as we grew out of this December-January bottom of the of the production curve.

I think what will be as [ph] – where are we (00:59:25) best positioned to invest in the business to grow or invest the business to maintain and utilize excess free cash to buy in debt or invest more in the business to grow – still growing business. So I think that's where the real inflection point is now as we're here. And now it's a question of, as we invest in this price environment, are we going to really look to grow very modestly or maintain flat production and try to buy in debt or pay down our debt with the excess free cash flow. I think, as you saw last year, we were still arresting our decline as we guided in. I think we would have obviously bottomed out except for the fires and the mudslides. So, at this point in time, I think we're back on that trajectory, as I alluded to before. I think by the end of this quarter and early Q2, you'll see us back up to where we should have been and continue to kind of maintain or grow modestly from there.

Joseph Von Meister
Analyst, Bennett Management Corp.
Q

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So, do you see an exit rate in Q1 of something closer to 128,000 BOE to 130,000 BOE?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

No. I think, obviously, we guided 120 MBOE to 125 MBOE. I think if you wanted to think that we should be closer to 125 MBOE, I think that that would be correct thinking at this point in time. But we have PSC effects that work against us also. So that's the wildcard when you think about on net production basis. So, if you didn't have any PSC effects, you – I would say, clearly, the way we guided out – but again, if we have prices meaningfully move up from here, it will meaningfully move the production down.

Joseph Von Meister
Analyst, Bennett Management Corp.
Q

Maybe it'd be good to report your numbers so that the PSC effects were included.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

Yeah. We have done that on a gross basis also and we do it in the guidance for the next quarter also, the attachment to the earnings release.

Marshall D. Smith
Chief Financial Officer & Senior Executive Vice President, California Resources Corp.
A

Yeah. If you look on page – it's Mark. If you look on page 21 of the press release, we give you the pricing effect, the PSC effects...

Joseph Von Meister
Analyst, Bennett Management Corp.
Q

Right.

Marshall D. Smith
Chief Financial Officer & Senior Executive Vice President, California Resources Corp.
A

...both on terms of production as well as production costs attributable to PSC effects at varying price scenarios, $10 up, $55, $65, $75. [indiscernible] (01:01:51)

Joseph Von Meister
Analyst, Bennett Management Corp.
Q

So the guidance that you're giving, I mean, just to wrap this up, and I apologize. But we're at 126,000 BOE in the fourth quarter, we were 128,000 BOE in the third quarter and we're expecting it to turn up. Now, you're guiding to 120,000 BOE to 125,000 BOE for the first quarter. And the disconnect or the problem that I have with that is that the mudslides only cost you [ph] 400,000 (01:02:17) barrels a day. So there's obviously something else going on or you're just being very conservative, I don't know.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.
A

No, the [ph] 400,000 barrels (01:02:27) a day was the net impact in the fourth quarter just from the December. I think if you look at the effects in January, they were higher than that. So when we look – we look at going forward, we think there's probably going to be overall effect going to be 2,000 to 3,000 barrels a day, plus or minus.

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Joseph Von Meister
Analyst, Bennett Management Corp.

Q

On a quarterly run rate?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. If you said that the quarter was December, January, February, it's going to be kind of that impact.

Joseph Von Meister
Analyst, Bennett Management Corp.

Q

Got it. Okay. So, this goes past and then you're sort of back to normal by the second quarter?

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Yeah. And that's really what we're talking about is that and the PSC effects, because if you look at – again, like I said, we still have a very small amount of our production that's offline, but there's a few hundred barrels a day of third-party production that we process at our gas plant in Ventura that was net production for ourselves also, that's still offline from the fires. So there's different impacts here going on.

Joseph Von Meister
Analyst, Bennett Management Corp.

Q

Got it. All right. Well, good luck, guys. Great progress. Thank you.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

A

Thank you.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Todd Stevens for any closing remarks.

Todd A. Stevens
President, Chief Executive Officer & Director, California Resources Corp.

Thank you, everyone. CRC is focused on value creation and our plan is working. We're enhancing our resource base to resume production growth while living within cash flow and expanding our margins, deliver long-term value for our partners and investors. These principles will continue to guide us through 2018 and beyond as we deliver much needed energy for California by Californians. As a reminder, we look forward to seeing you at our Analyst and Investor Day in New York on October 3. We expect to see a save the date from our Investor Relations team soon. Thank you and good-bye.

Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

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