THOMSON REUTERS STREETEVENTS

# EDITED TRANSCRIPT

CRC - Q4 2016 California Resources Corp Earnings Call

EVENT DATE/TIME: FEBRUARY 16, 2017 / 10:00PM GMT

## CORPORATE PARTICIPANTS

**Scott Espenshade** *California Resources Corporation - VP of IR*

**Todd Stevens** *California Resources Corporation - President & CEO*

**Mark Smith** *California Resources Corporation - SEVP, CFO*

## CONFERENCE CALL PARTICIPANTS

**Evan Calio** *Morgan Stanley - Analyst*

**Doug Leggate** *BofA Merrill Lynch - Analyst*

**Brian Singer** *Goldman Sachs - Analyst*

**John Herrlin** *Societe Generele Corporate and Investment Bank - Analyst*

**James Spicer** *Wells Fargo Securities - Analyst*

**Pavel Molchanov** *Raymond James - Analyst*

**Sean Sneeden** *Oppenheimer & Co. - Analyst*

**Unidentifed Participant** *- Analyst*

## PRESENTATION

**Operator**

Good day everyone, and welcome to the California Resources Corporation fourth-quarter and 2016 earnings conference call.

(Operator Instructions)

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

---

**Scott Espenshade** - *California Resources Corporation - VP of IR*

Thank you, I'm Scott Espenshade, Vice President of Investor Relations. Welcome to California Resources Corporation's fourth-quarter and full-year 2016 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 the CRC executive team. I would like to highlight that we've provided slides in our investor relation section of our website, www.crc.com.

These slides provide additional insight into our operations and fourth-quarter results, and reserves information. Also, information reconciling non-GAAP financial measures discussed to their most directly comparable GAAP financial measures are is available in the investor relations portions of our website and in our earnings release. Today's conference call contains certain projections and forward-looking statements within the meanings of federal securities 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 on the Company's 10K which is being filed later this month. We ask that you will review it when available, and the cautionary statements in our earnings release.

A replay and transcript will be made available on our website following today's call and will be available for at least 30 days following the call. I want to note we are hosting in analyst day and site tour on March 22 in Bakersfield at our Elk Hills facility and also a visit to our Wilmington Field in Long Beach on March 23.

We believe this will be a great opportunity to see some steam flood and water flood assets firsthand as well as learn more about our 2017 plans, assets and our VCI process in more detail. Please note that we have limited space available to travel logistics and safety considerations. We also plan to webcast the analyst day presentation and will post a webcast link and accompanying slides to our website at our earliest opportunity.

As a reminder, we have allotted similar times for earnings Q&A at the end of our prepared remarks. I would ask that participants limit their questions to a primary and a follow-up question. I will now turn the call over to Todd.

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Thank you, Scott. Thank you, everyone, for attending CRC's year end 2016 earnings call. We are at an inflection point with our activity levels and we enter 2017 well positioned to move from defense to offense.

We believe our asset base can generate high single-digit production growth and EBITDAX growth of over 20% with solid margins over multiple years. Our confidence is rooted in diligent execution by our team, the quality of our assets, and the flexibility of our business model. Our 2016 results demonstrate that at CRC we do what we say we will do.

We've always said we are focused on value. This past year we determined the best way to deliver value through the down cycle was to pull back capital and preserve the optionality of our asset base. This decision, coupled with our low decline asset base and low development costs, showcase the resilience in capital efficiency of our portfolio.

We closed the year with production above our expectations, meaningful debt reduction, higher actionable joint inventory and more efficient operations. We did all this through a generational downturn for our industry. Going forward, we intend to continue living within cash flow while making high-value investments in our asset base and to continue strengthening the balance sheet opportunistically in ways that optimize value for our shareholders. As such, I'm highly confident that the best is yet to come for CRC.

For 2017 we have increased our annual investment plan for the first time since the spin. We are beginning year with a $300 million budget that should provide essentially flat production this year and return us to a growth profile in the second half of the year. We will also move our priorities from the right-hand side of the balance sheet to the left side, with investment and assets to help us strengthen our balance sheet organically.

Today we have achieved the majority of our deleveraging through liability management opportunities. As our debt has continued to trade higher, the opportunity capture discounts in our debt is limited. Therefore we're focused on deleveraging through EBITDA growth.

We have a large inventory of high-graded projects and we believe we can now unlock more value and delever more quickly by developing our assets to spur that growth. In addition, we will continue to pursue opportunities such as joint ventures or other potential monetizations that accelerate production growth, increase cash flows, help do derisk our portfolio, and potentially deleverage if the value proposition is right for CRC.

Today we announced a key step in this direction with an up to $250 million joint venture with Benefit Street Partners which provides incremental capital to our $300 million capital program. The initial commitment a $50 million by our partner will be invested to accelerate development in the San Joaquin basin through the summer. We expect to invest up to additional $100 million of the JV capital by the end of the year subject to JV partner approval. With a significant portion of JV capital been invested in the second half of the year, we expect an uplift in our 2017 production exit rate with a full production upside coming in 2018.

We further believe the JV will provide modest net positive cash flow this year. We are also in discussions with several potential joint venture partners, who we believe recognize a diverse expiration in development value proposition of our resource base here in California. Let's now revisit the highlights of 2016.

First and foremost since the spin, strengthening the balance sheet has been our key focus. In 2016 we proactively reduced our debt by $900 million, as detailed in the slides. We chose to strengthen our balance sheet through liability management activities at an overall financial cost, which is significantly lower than it would have been achieved through an asset monetization.

This option also provide a better value than selling material producing our infrastructure assets at the bottom of the cycle. We have not pursued any substantive dilutive transaction as a part of our balance sheet efforts and don't intend use equity for debt reductions, unless we believe the outcome would enhance underlying long-term shareholder value.

Going forward we will continue to focus on identifying, evaluating, and pursuing value creation opportunities that strengthen our balance sheet and reduce our financial leverage. One of our major themes in 2016 was to maintain the base.

Our team has done a tremendous job with their surveillance of our base production. With essentially no capital applied to production enhancement in many fields we experience the actual decline rates of CRC's assets not just calculated academic rate. We focused on maximizing the uptime of our 8,800 active producing wells to make sure they are capable of producing at their most efficient level.

Showcasing our knowledge of the assets and complimentary infrastructure we further improved our uptime record by emphasizing proactive maintenance programs. Through this effort we achieved a corporate decline rate consistent with our guidance of less than 13%. Fourth-quarter volumes represented a 10% year-over-year decline excluding PFC effects.

In addition, CRC's operations again delivered exceptional safety and environmental performance, receiving recognition from the National Safety Council and the Wildlife Habitat Council. This is validation of our commitment to being the operator choice in California.

Another key theme has been to protect our margins. We've developed an entrepreneurial culture at CRC that has taken root in the entire organization. This development has fostered many new ideas to protect our margins.

Our teams have reduced field operating cost by 16% this past year, and 22% since the spin in 2014. A significant portion of these reductions resulted from process improvements that should continue to benefit us. We do expect to see modest inflation from increasing energy costs indirectly or directly in the form of higher natural gas prices.

However, higher natural gas prices are a net positive for our margins as increased revenues from a gas production's more than offset elevated operating costs. Our marketing team has built a hedging program that has enhanced our realized prices by $77 million in 2016. In addition, we continue to pursue multiple market outlets to maximize our realization.

Protecting our margins involves both cost and revenue sides of the equation and we will continue to work on both of 2017. We will strive to control costs in line with the second half of 2016, but will see costs creep higher due to natural gas prices and lower production levels in the first half of 2017. As we consider new investments we prioritize projects and allocate capital using our value creation index, or VCI, a metric we used optimize returns on invested capital.

Using VCI in the second half of 2016 we directed capital largely to low cost, high return capital work over projects, which further reduce the decline rate and enhanced our capital efficiency. Our work on reliability and surveillance programs mitigated our already low decline. Our production level, even with minimal capital investment, confirms the powerful combination of the strength of our diverse assets and our VCI formula. A proven differentiator from our peers even as past years' volatile price environment.

Our teams have also expanded and high graded our actionable inventory, in the beginning of 2016 brought our drilling activity to a halt. Our technical teams took advantage of the pause and joined to take a fresh look at our life of field development plans for many of the fields. This review significantly increased our actionable inventory by uncovering new locations, revising development plans, further reducing development costs and identifying additional work over candidates.

In total, our teams have doubled the capital we can deploy to drillable and actionable investment opportunities that meet our 1.3 VCI hurdle at $55 Brent and have significantly increased inventory at higher price points. Importantly we have grown our probable and possible reserves by 420 million barrels, 130% increase since the spin despite prices dropping by approximately half. These actions will provide a ready source of projects as our annual cash flow increases at about current or higher prices and will provide ample opportunities to accelerate future development through the potential joint venture agreements.

Our enhanced life of field development plans and better-than-expected well performative allowed us to replace 71% of our production, excluding the effects of price adjustments, despite a very limited capital program. This resulted in organic F&D before price related revision of $3.42 per BOE in 2016. This is the second year in a row that our organic F&D costs have been in low single digits resulting in a recycle ratio of 3 times.

We provided several planning scenarios publicly in our third quarter call that highlighted a number of potential future outcomes. These planning scenarios show that by reinvesting all of our annual pre-cash flow we believe we can grow our oil production in a high single-digit CAGR using analyst consensus pricing at the time, and assuming modest cost inflation and development risk. More impressively these planning scenarios suggest an EBITDAX growth at a mid 20% CAGR with these assumptions.

Our fourth-quarter operating results combined with improving and stabilizing commodity prices indicated that we are positioned for cash flow production and reserve growth both on a debt adjusted per-share basis. We believe we can deliver this result by focusing our capital and oil projects that provide high margins and low decline rates. These factors collectively should generate compounding cash flow over our planning horizon.

As I mentioned, we are beginning the year with the $300 million capital budget which we plan to fund from operations, assuming prices remain at about current levels and cost inflation is modest. Under this plan we project we will arrest our oil production decline by roughly mid year and start growing in the second half. As a result we anticipate our 2017 BOE exit rate to be comparable to our entry rate.

Our 2017 capital plan will focus primarily on crude oil development and delineation projects in some of our largest deals. Elk Hills, Wilmington, Kern Front, Buena Vista, and Kettleman North Dome will see the majority of the capital investment that will be focused on capital workovers and new conventional, unconventional and injection wells.

We expect this program to deliver an overall VCI approaching 3 at current prices. That means nearly $3 generated after cost of capital over the life of the project for every $1 invested. Given the volatility we have experienced in prices over the last two years, we have developed executable alternative cash flow mutual plans for 2017 which range from under $100 million, which would focus mostly on capital workover safety and mechanical integrity projects and modest drilling, to $500 million in a higher price environment and subject to the approval of our Board. There is still meaningful excess capacity in the California service and supply sector, which we expect will allow us to maintain the deflationary portion of the cost reductions we have seen over the last two years until industry activity in California returns to significantly higher levels.

Our planning scenarios show that at about current or higher oil prices we can strengthen our financial position faster by redeploying our cash flows into operations rather than paying down debt. However, we will monitor the market for opportunities to either the redeploy our cash flow into operations, or into debt reduction based on each alternative's underlying value proposition.

We delivered on all of their key tenets last year and are focused on effectively communicating these achievements in the market. We believe that our equity is still significantly undervalued.

Currently our stock is more representative of an option on crude rather than reflecting the underlying value of CRC. We expect to demonstrate the Company's full value as our margins expand and cash flows increase. I will now turn the call over to Mark to discuss the details of our fourth-quarter and full-year results.

---

**Mark Smith** - *California Resources Corporation - SEVP, CFO*

Thanks, Todd. In 2016 we executed strongly on our commitments. We've demonstrated we can reduce debt and production without shareholder dilution, all while living within our cash flow.

For the year we generated $49 million in pre-cash flow after capital reflecting our value focused disciplined approach to investment. Additionally, we reduced our debt levels by roughly $900 million. Cumulatively, we have reduced debt by nearly $1.5 billion from peak levels.

Our team accomplished this through a combination of the debt exchange, open market purchases, Limited debt through equity swaps, a cash tender, and importantly, free cash flow. I want to point out that we accomplished this without selling any significant assets at the low end of the cycle and with only a minimal increase in the ongoing cash cost to the Company. Along with our financial tenets, we accomplished our operational tenet of minimizing our base decline with nominal capital.

As Todd mentioned, CRC continued its strong legacy of safety and environmental stewardship, demonstrating stellar 2016 performance. For full-year 2016 production came in at 140,000 barrels of oil equivalent per day, reflecting a modest decline of just 12.5%.

In fact, excluding PSC effects, our corporate decline would have been under the 12%. Oil prices recovered in the fourth quarter of 2016 with the Brent index averaging $51.13 per barrel compared with multi-decade lows earlier in the year. We are cautiously optimistic that the fourth quarter is a turning point toward a more stabilized, relatively higher commodity price environment.

Reflecting the increase in Brent, the fourth quarter realized crude price of $45.48 including cash hedges with 6% higher than the prior quarter and 1% lower than the prior year period. For the 2016 quarter, cash hedges decreased our realized price by $1.12 per barrel due to higher commodity price environment compared to market expectations when we implemented the hedges. Despite the strong prices in the fourth quarter, the cycle's apparent trough prices earlier in the year resulted in full year 2016 realized crude price of $42.01 per barrel including the effects of cash hedges. Cash hedges contributed $2.29 per barrel to our realized price for the full year of 2016 compared to $2.04 per barrel for 2015. Our realized NGL prices for the fourth quarter and full-year 2016 were $28.99 per barrel and $22.39 per barrel respectively.

Strong liquids exports as well as a colder start to the winter season in much of the country drove 48% and 14% increases from the prior year quarter and the prior year respectively. Our realized natural gas price for the fourth quarter of 2016 was $2.79 per MCF which was up $2.44 in the prior year period. The quarter over quarter increase in price was driven by higher US exports, a colder start to the winter season, and specifically in Southern California, the effect of limited storage caused by third-party disruptions that began last winter.

Similar to the decline in crude prices our full-year 2016 realized price declined 14% to $2.28 per MCF, down from the $2.66 registered in 2015. Our business model provides flexibility because we have a portfolio of assets across multiple drive mechanisms as well as complementary infrastructure. So the sustained increase in crude prices after the first quarter of 2016 gave us the confidence to gradually increase our capital investment during the second half of the year.

As a result, fourth-quarter capital of $31 million was higher than each of the prior 2016 quarters. You'll recall early in the year we officially put a hold on development capital plans to monitor the depth of the downturn before we increased our investment alignment with our cash flow. Our drilling program was reactivated in August with one rig working in the San Joaquin Basin focused on steam floods and water floods and a part-time rig in the Los Angeles basin at the Wilmington Field through your end.

For the full year we completed 42 wells, of which 34 were steam flood wells and eight were water flood wells. In addition, as Todd noted, capital workover projects typically have a relatively high VCI, and we performed 130 capital workovers during the year. In total of full-year capital investment was $75 million, which was well within our cash flow for the year.

As I previously mentioned, production volumes for the full year of 2016 averaged 140,000 barrels of oil equivalent a day. Our decision the pull back capital due to lower commodity prices negatively impacted our share of production from our production sharing contracts at our Long Beach operations by 1000 BOE per day. Excluding this PFC effect our year-over-year production decline would of been under 12%.

For the fourth quarter of 2016 production volumes were 135,000 BOE per day, which was just 2% lower sequentially and down 10% year-over-year excluding the PFC effect. The lower sequential decline reflects the combination of a flatter than estimated base decline rate and resumption of a modest capital program which together are moderating our corporate decline rate.

Reflecting our focus on oil projects, full-year oil production of 91,000 barrels per day would have been under just 12% below average 2015 levels excluding the PFC effect. Full-year average NGL production decreased 11% year-over-year while full-year natural gas production declined 14% from the 2015 average.

Todd mentioned a solid execution by CRC's team in a challenging year. Our team delivered a meaningful reduction in our production costs, a critical aspect of our 2016 success. We successfully reduced field operating costs by approximately 22% since the spinoff, largely by applying modern technologies and operating methods to develop our assets and improve operating efficiencies.

Full-year 2016 production costs came in at $800 million, or $15.61 per BOE compared with $951 million or $16.30 per BOE for 2015. This 2016 cost reduction represented a16% decline on a dollar basis and a 4% decline on a BOE basis. Of the dollar reduction, proximally 25% related to lower energy cost, while the balance came from all categories including surface operations, down home maintenance and labor costs.

Fourth quarter 2016 production costs came in at $217 million or $17.50 per BOE compared with $221 million or $15.51 per BOE in the prior year period. Our fourth-quarter 2016 production costs were higher because of $10 million in compensation expense adjustments which reflected the effect of the recent strong increase in our stock price in related items.

On an absolute dollar basis, fourth-quarter 2016 production costs were $6 million higher compared to the third quarter 2016, largely due to this compensation expense adjustment. Our cost reduction focus extended general administrative and exploration expenses as well. Adjusted G&A expenses for the full year of 2016 were $228 million compared with $287 million for full-year 2015.

Fourth-quarter 2016 adjusted G&A expenses were $61 million compared with $69 million for the fourth quarter 2015 reflecting workforce reductions. These decreases represented a 21% decline on the full-year basis and a 12% decline on year-over-year quarterly basis. Compared to the third quarter of 2016 fourth-quarter adjusted G&A expenses were slightly higher due to higher accrual for employee compensation resulting in part of the strong increase in our stock price in the fourth quarter of 2016.

Exploration expenses for the full year 2016 were down $13 million to $23 million. This includes $10 million for the fourth quarter. The full-year decrease was result of our actions in lease rentals as well as lower exploration activity.

Taxes other than on income, which largely consist of property taxes, were lower on the full-year as well as a quarterly basis compared to 2015. We benefited from lower assessed property values due to the downturn of commodity prices in 2015. As in prior quarters, DD&A expense for the fourth quarter and full-year of 2016 were significantly lower than the comparable 2015 period due to our 2015 impairment charge. Interest expense of $85 million for the fourth quarter of 2016 was slightly higher than the fourth quarter of 2015 due to higher blended interest rates resulting from the liability management actions that we've taken today.

For the fourth quarter of 2016 we've reported a net loss of $77 million or $1.83 per diluted share. The adjusted net loss of $74 million, or $1.76 per diluted share reflected a 4% decrease from the comparable 2015 period on an absolute basis. Full-year 2016 net income registered $279 million or $6.76 per diluted share. The adjusted net loss of $317 million or $7.85 per share for 2016 was down 2% from the adjusted net loss of $311 million or $8.12 per share for 2015. We have noted the detailed analysis for you in our press release.

Adjusted EBITDAX for the quarter for the fourth quarter of 2016 was $168 million and $616 million for the full year. Current year amounts were lower than the $226 million and $906 million registered in 2015 and reflected the lower commodity price environment and lower production, partially offset by our success in lowering our overall cost structure.

Operating cash flow for the full year of 2016 was $130 million and we generated $49 million of free cash flow after working capital for the full year of 2016, again, demonstrating our ability to live within our means. Additionally we sold a small property this month for just over $30 million.

Many people have contributed to CRC's success this past year, I would like to personally thank CRC employees for their vital contributions. I would also like to express our appreciation to our banks for recognizing CRC's unique asset base and working with this during this prolonged downturn.

To that end, our banks just approved a sixth amendment that removes a capital investment limitation. The amendment provides additional flexibility to execute joint ventures such as the recent joint venture agreement that Todd discussed earlier.

In closing, I want to highlight CRC's accomplishment of reducing debt by nearly $1.5 billion from peak levels during a down market and still being free cash flow positive. We were able to accomplish this with our disciplined value creation approach. We had strong results in a very difficult year and we believe if 2017 provides the price stability it has so far we can deliver solid margins as well as value.

Please note that we've provided key first quarter 2017 guidance information in the attachments to our earnings release. Our guidance includes the small recent effect of weather on our operations, which mainly affected the movement of equipment in the field.

I will be happy to take any questions you may have on that information on other aspects of our results during the Q&A portion of call. I will now turn it back over to Todd.

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Thank you, Mark. In 2016, in a very demanding environment, our organization executed successfully on the objectives that were within our control. Even during this challenging period we did not waver from our vision of providing Californians with needed, ample, affordable and reliable energy.

CRC enters 2017 well positioned to move from defense to offense as we execute against our large inventory of projects to deliver value for shareholders. We are excited about 2017 because of our exceptional capital efficient asset base, the flexibility of our business model, and the skill and dedication of our people.

At CRC we embody California's frontier spirit. We don't just aim to preserve value, we push to discover, create and develop the rich opportunities we have before us to benefit all of our shareholders.

This concludes our prepared remarks, and we now welcome your questions.

---

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions)

The first questioner today is Evan Calio with Morgan Stanley. Please go ahead.

---

**Evan Calio** - *Morgan Stanley - Analyst*

Good evening guys. My first question, you guys established the 2017 CapEx at your maintenance CapEx level.

You have free cash flow at the strip on that amount. So how should we assume it's redeployed in 2017? I'm just trying to understand, the direct deleveraging potential versus the deleveraging through growth that you mentioned, to reach a more sustainable capital structure?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

What we have outlined here is a plan that, for about $300 million investment, excluding the joint venture where we're going to be from a production standpoint flat from entry to exit. And we believe we will be again [free cash] flow neutral for the year, but that also includes we're amortizing $100 million of the term loan during the year too.

**Evan Calio** - *Morgan Stanley - Analyst*

Okay, I get that. Okay. And then maybe, the second is -- congrats on the JV.

Can you discuss how that JV is structured in terms of partner payouts? And is that your $50 million -- I guess, the first payment considered in your CapEx figure?

**Todd Stevens** - *California Resources Corporation - President & CEO*

It is not in $300 million, it will be incremental. And we outlined where we feel like -- we've outlined plans where we can ramp up production to $500 million for this year of capital investment. So we feel fairly confident we'll be able to show you this in March 22 at our Analyst day, all the details behind, not just our $300 million plan, but the incremental plan including the partnership with the Benefit Street.

The way its structured with them is it's primarily investments in the San Joaquin Basin, and it targets a low teens rate of return for them. And then there's a -- then they get an exit with no residual after that point in time. And they, effectively carry us on 100% of the capital.

**Evan Calio** - *Morgan Stanley - Analyst*

But you said, but you're getting -- you're saying you get cash payment in 2017. So I guess, it doesn't pay them out to their return, in the first year, it's over time? Or how does that work?

**Todd Stevens** - *California Resources Corporation - President & CEO*

No, it's definitely over time. We think it will be modestly cash flow positive for us, primarily in the back half of the year as we get to investing the capital. But yes, we don't think you get full benefit from the cash flows until -- full benefit from the production arguably too, until you get more into 2018.

**Evan Calio** - *Morgan Stanley - Analyst*

Okay, I'll leave it for somebody else, thanks.

**Todd Stevens** - *California Resources Corporation - President & CEO*

Thanks.

**Operator**

The next questioner today is Doug Leggate with Bank of America Merrill Lynch, please go ahead.

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Thanks, good morning or afternoon, everybody. And also congrats from me, [to all of you on] getting your first one done Just a point of clarification is my first question on the production gate. Does the move to four rigs include the incremental activity associated with the joint venture?

**Todd Stevens** - *California Resources Corporation - President & CEO*

No.

---

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

So what would incremental activity look like beyond the four net to CRC?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Immediately I think as we look to draw down the first tranche, it will probably add one rig, and it could add two rigs in the back half of the year.

---

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Okay, so it's incremental to your production guide as well?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

I think, in production, it will be incremental to our production, yes. We will definitely exit the year, more than we entered the year with the joint venture.

---

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

Okay. Now my follow up is, and I'm guessing you're trying to hold some of this back for the Analyst Day, but it sounds like the shape of your production is down a little bit in first half, and obviously you said, (inaudible) go up in the second half. But to Evan's point, on a maintenance capital budget, that would put you on a growth exit, if you like coming out of 2017. So I guess, what I'm asking is, what is the [implication] if you can grow the second half at this capital budget, what does that mean about your maintenance capital, has that come down again? Are you not able to grow it beyond the [$100 million]? And I'll leave it there. Thanks.

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Yes, I think what it says is we're arresting our decline mid year. As you know when you invest in our business, typically you don't get immediate results. So we're arresting the decline from the lack of investment, the last arguably two years.

We think that will occur somewhere around mid year, and then we start growing the business. I still think if you thought about again, instead of talking about one individual year, if you talk about three to five year horizon, our maintenance CapEx is going to be between $300 million and $400 million, and more biased toward the lower end. But like I've told you before, any particular year could be substantially lower depending on the project mix that year.

---

**Doug Leggate** - *BofA Merrill Lynch - Analyst*

All right, great progress. I'll leave it there. Thanks so much.

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Thank you.

**Operator**

The next question is from Brian Singer with Goldman Sachs, please go ahead.

**Brian Singer** - *Goldman Sachs - Analyst*

Thank you, good afternoon. Your scenario on slide 7 assumes that all the cash flow is reinvested, and this may be a little bit of a similar line to Evan's question. But when you think about the balance sheet, is your goal simply to keep debt flat or to reduce it? While $65 oil would certainly be very welcomed, what type of contingency planning are you doing, if that's not the case, and we stay around current levels?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Yes, so from our standpoint, we, on that particular slide, again we used this consensus pricing at the time. We looked at our plan, and looked at the best value proposition given the dearth of opportunity, given by the [liability] management, and how our debt traded, that the best opportunity to create value for our shareholders was to invest in the business. And in going forward, we want to articulate our plan that we can grow it long-term, into our debt organically at the current prices around the current strip.

And so from our standpoint, Mark and I have said many times, we would like to have a leverage of about 2.5 to 3 times. And you can get there a variety of ways. One, you can grow the numerator or denominator, or take away from them.

So we are going to try and grow into the debt. Obviously, just like we were during the last few years, we will be opportunistic. If opportunities present themselves for real value to delever, or to invest in something else with our cash flow in the business, whether it be in our E&P or our power plant, or whatever, we will take advantage of those opportunities. But to date our best value proposition is to organically invest and continue to drive that train to get there.

**Brian Singer** - *Goldman Sachs - Analyst*

Got it. Thanks And then I have a follow-up on the JV, andI may not have heard it right.

But is this a JV where you end up having to buy the wells back after the partner receives a certain rate of return? Or is this an investment for the life of well? Maybe you could add a little bit more color on that, on the process here?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Effectively there's a reversionary feature once they reach a threshold return. And at that point in time, there is no residual impact for the enterprise.

**Brian Singer** - *Goldman Sachs - Analyst*

I'm sorry, that means you would end up receiving a greater working interest in those wells, or the working interest would switch, or you have to buy the wells back at PDP?

**Todd Stevens** - *California Resources Corporation - President & CEO*

No, they would just revert at that point in time. And they would, at that point in time they would be out of it, and it would be our 100% or whatever our working interest or net revenue was at that point in time.

**Brian Singer** - *Goldman Sachs - Analyst*

Okay. Got it, so no outflow or anything at the end?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Correct.

**Brian Singer** - *Goldman Sachs - Analyst*

Okay. Thank you very much.

**Operator**

The next question comes from John Herrlin with Societe Generale, please go ahead.

**John Herrlin** - *Societe Generele Corporate and Investment Bank - Analyst*

Todd, could you address how this JV came about? Are any properties exempt, how do you decide to throw something into the JV?

**Todd Stevens** - *California Resources Corporation - President & CEO*

I think when we looked at it, it came about -- we've been talking to people about joint ventures, really almost since inception, exploration, development joint ventures. This came about over the last few months and we had active discussions with Benefit Street, and we felt like it was a good mix for us, to help accelerate resource forward, that in some cases we wouldn't have gotten to for a few years, or things that are probable and possible and the like, and some PUDs, that we could partner together to get their return objectives met, and get our value proposition met.

To give you scale, we feel like this joint venture, if executed like we think today, in today's price environment generates over $5 of value for the CRC shareholder. And it gets Benefit Street's investors their return they need.

**John Herrlin** - *Societe Generele Corporate and Investment Bank - Analyst*

Okay. Next for me, with the MLP market kind of opening up, what about your infrastructure?

**Mark Smith** - *California Resources Corporation - SEVP, CFO*

We continue to monitor that, and we will do what makes sense and creates the most value. If something comes along that makes a lot of sense from an MLP or any other kind of asset monetization with our infrastructure, we will take a hard look at it, and see if it creates the most value for our shareholders and if it's the best proposition. It could be a way for us to quickly, more quickly delever. But again, we are not holding any fire sales, we're going to do what makes sense.

**John Herrlin** - *Societe Generele Corporate and Investment Bank - Analyst*

Great. Thanks, Doug.

**Mark Smith** - *California Resources Corporation - SEVP, CFO*

Thanks John.

**Operator**

The next questioner is James Spicer with Wells Fargo, please go ahead.

**James Spicer** - *Wells Fargo Securities - Analyst*

Hello, good afternoon. I noticed that you were able to get the restrictive CapEx covenants removed under your credit facility. Wondering what other changes may have been made to the credit facility?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Yes, James, I will let Mark go ahead and handle that.

**Mark Smith** - *California Resources Corporation - SEVP, CFO*

Hey, James, this is Mark. Primary provisions of the amendment were first to eliminate the investment limitations that you described. In exchange, we incorporated the liquidity covenant, which is essentially consistent with the way in which we manage the business in terms of minimum liquidity, allowed us to do the of joint venture that we talked about, and then some other miscellaneous provisions. But the key things were, the ability to do the JV, and the ability to continue to invest in the business like Todd described just a minute ago.

**James Spicer** - *Wells Fargo Securities - Analyst*

What was that minimum liquidity amendment that you were -- that you just mentioned?

**Mark Smith** - *California Resources Corporation - SEVP, CFO*

The minimum liquidity requirement of $250 million.

**James Spicer** - *Wells Fargo Securities - Analyst*

$250 million, all right, thank you. And then secondly, I was just wondering if you could talk a little bit more about operating costs and the sort of progression here? It looks like you around $17.50 in the fourth quarter, and you mentioned that a portion of that was due to increased share compensation expense. And I see that you're guiding to higher production costs in 2017. Maybe just discuss what's leading to the -- what's the different pressures are that are driving things higher?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Yes, I think it's pretty simple. When you look at, an absolute basis from the fourth quarter to the first quarter on operating costs, on an absolute basis is actually coming down, we have declining production, that like we said we feel like we will arrest by mid year.

We also have higher natural gas prices, but the unique element there is it might be higher than the cost line, from the gas prices we enjoyed last year, but it will be even higher from a margin perspective on the revenue line for ourselves, because we are net long natural gas.

So those are the primary contributing factors that you're going to see going into the year. Also you've got to remember in the back half of the year, if you want to compare it to the front half of the year, we essentially had limited to no workover activity. It was really just mechanical integrity, and health and environmental and safety work being done.

And then we got back to downhole maintenance and the like, and getting back on production. So you will see more in that expense line also, but that comes with a direct benefit because in most cases you're putting back production on.

---

**James Spicer** - *Wells Fargo Securities - Analyst*

Okay, that makes sense. Thank you.

---

**Operator**

The next questioner today is Pavel Molchanov with Raymond James, please go ahead.

---

**Pavel Molchanov** - *Raymond James - Analyst*

Thanks for taking the question, guys. It's been a while since anyone has had to ask you about well permits. But given that you are getting back to a drilling program, what is the latest on timing, ease of getting permits, whether on the water floods or on the conventional assets?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

As we've talked about this before, I think all of our inventory that we are focusing on for this year in the capital budget, whether be $500 million or a $100 million is actionable inventory for us. So we are working on the permits. They are usually longer lead time.

I mean, that's what we've always said. In California, usually you end up getting the permits, it just takes a little longer than elsewhere, because you have more planning to do up front.

So from our perspective, is it perfect? No. But I think we are in pretty good shape, and we understand how we're executing and getting permits in the space.

---

**Pavel Molchanov** - *Raymond James - Analyst*

Okay. Can you just clarify one thing about the guidance? So when you talk about getting back to production growth, second half of the year, is that only in reference to oil, or is that total output?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

I'd say it's oil-focused, but I think, we'll really -- gas will be arrested, it won't decline as rapidly.

---

**Pavel Molchanov** - *Raymond James - Analyst*

Okay, so on a BOE basis, will you be growing by the end of the year?

**Todd Stevens** - *California Resources Corporation - President & CEO*

Yes, that's what brings us back to entry to exit being flat.

**Pavel Molchanov** - *Raymond James - Analyst*

Okay. I appreciate it.

**Operator**

The next questioner is Sean Sneeden with Oppenheimer, please go ahead.

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

Hello, thank you for taking the questions.

**Todd Stevens** - *California Resources Corporation - President & CEO*

Hello Sean.

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

Todd, I know you had mentioned that on average, I think the projects that you guys are allocating capital towards this year are roughly a [3 VCI], I think on average. I know you guys outlined your new or updated inventory on slide 17. Can you just give us a sense of how much of your inventory in that figure, or in those figures are [3 VCI] or better?

**Todd Stevens** - *California Resources Corporation - President & CEO*

What VCI or better, sorry? A 3?

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

[3], yes.

**Todd Stevens** - *California Resources Corporation - President & CEO*

I don't know if we've got it broke down by that or not, but we have a fair amount. In this program to give you scale this year, it's not all workovers, there's a fair amount of -- over half the $300 million is going to drilling and workovers.

And this isn't -- in some cases this is more drilling of probables and possibles, than it is drilling a PUD offset one location. So I, going forward, I'd say we have a fair amount as price contingent.

But at the current prices, we probably still have quite a bit that is above [3]. I don't think we haven't broken out that way.

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

Okay, no, that's fine. I guess, just thinking about the balance sheet. You had mentioned some of your deleveraging targets and trying to get back to 2.5 to 3 times. How are you thinking about the stub pieces of the unsecured notes at this point? I guess, the first maturity there is in 2020. How are you guys generally thinking about trying to address those?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

Well, I think obviously we are not going to get to 2020 and address them, I think we will be very proactive on how we might engage in that. I think we see it through a kind of a master plan here, that would deal with many issues at that point in time, because we have a revolver and some of our unsecured is coming due at a very similar time frame, so along with our term loan.

So I think from our perspective you'd see us do a very comprehensive solution at some point in time. I wouldn't wait -- we obviously wouldn't wait until the last minute to get it done.

---

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

Okay, that makes sense. If you don't mind, just squeeze one housekeeping question in. Just give us a sense of what type of working interest Benefit Street gets in the JV at the outset, are they getting 100% of the well, or can you give us a sense of what that looks like?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

They will get a portion, and it's a small portion, but I would say, it's not necessarily a working interest. It's more of a net profits interest.

---

**Sean Sneeden** - *Oppenheimer & Co. - Analyst*

Okay, got it. Thank you very much.

---

**Operator**

The next questioner is Tarek Hamid with JPMorgan, please go ahead.

---

**Unidentifed Participant** - *- Analyst*

Hi, this is Kevin actually calling in for Tarek, I appreciate you guys taking the call. Just on your -- you mentioned that you guys have a few JV opportunities potentially down the pipeline.

Just want to see how we should think about capital growth going forward? How much of that should be funded through JVs, versus more internally?

---

**Todd Stevens** - *California Resources Corporation - President & CEO*

When you look at it, I think you could probably make some calculations on our cash flow generation capacity. And assume at this point in time, the best value proposition for our shareholders is reinvesting in our asset base, as this year with the [3 VCI] project. And incremental to that will be our partners that we might have like Benefit Street or others, that could be partners that do development or exploration joint ventures and different types of development joint ventures.

**Unidentifed Participant** - - *Analyst*

Okay, and I guess just to follow-up on that. In the past you guys have been a little bit more cautious to put up some of your assets for sale. Has that view kind of changed with the current environment? Any new developments on potential divestitures?

**Todd Stevens** - *California Resources Corporation - President & CEO*

As you heard, Mark announce, we sold a small property, we thought after careful analysis was non-core to us. So we continue to look at our portfolio for opportunities to divest things that makes sense and are accretive to our shareholders. Nothing is off the table from our perspective. We'll look at any kind of asset monetization. But again, going back to what I said earlier, we're not holding fire sales, we will look at things that create value for our shareholders longer term.

**Unidentifed Participant** - - *Analyst*

Okay. That's great, thanks guys.

**Operator**

This will conclude the question and answer session. I would like to turn the conference back over to Todd Stevens for any closing remarks.

**Todd Stevens** - *California Resources Corporation - President & CEO*

Thank you everyone. We are looking forward to seeing you in March, in a month from now in Bakersfield, and talk about our 2017 plans, and what we have in store, here at California Resources. Please give us a call here in Los Angeles with any questions. Thank you very much.

**Operator**

The conference is now concluded. Thank you all for attending today's presentation, you may now disconnect your lines.