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## Conference Call Transcript

**UCL - Q3 2004 Unocal Earnings Conference Call**

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## CONFERENCE CALL PARTICIPANTS

**Fred Leuffer***Bear Stearns - Analyst***John Herrlin***Merrill Lynch - Analyst***Steve Enger***Petrie Parker - Analyst***Phil Pace***Credit Suisse First Boston - Analyst***Mark Gillman***Benchmark Co - Analyst***Albert Anton***Karl H Forsheimer - Analyst***Gail Yen***Smith Barney - Analyst***Rahan Rasheed (ph)***FBR - Analyst***Michael Prince***Blue Star Industries - Analyst*

## PRESENTATION

**Operator**

Once again, all participants standing by for third quarter conference call please continue to stand by. Your teleconference will begin momentarily. Good afternoon and welcome to today's Unocal third quarter conference call. Following today's presentation there will be a formal question and answer session. At that time instructions will be given. Until that time all lines will remain in a listen-only mode. At the request of Unocal today's teleconference will be recorded. Any objections you may disconnect at this time. I would now like to turn call over to your conference host, Mr. Robert Wright. Sir, you may begin when ready.

**Robert Wright - Unocal**

Thank you, Anita. A replay of this audio broadcast will be available through our website and over the telephone. Please call the Investor Relations group in either El Segundo or Sugar Land if you have any questions. There are some slides available for you to view as a supplement to what is mentioned on call. You can review the slides on the Unocal website at [www.unocal.com](http://www.unocal.com). As we progress through the call, some of the slides will be referenced by number. Some are provided for backup purposes only. Our presentation today including these slides contains forward-looking statements and non-GAAP financial measures.

Please refer to slide two for a cautionary note regarding forward-looking statements, and for the location of the reconciliation and other information regarding the non-GAAP financial measures. Joining me on call today is Chuck Williamson, Chairman and CEO; Joe Bryant, President and COO; and Terry Dallas, our Executive Vice President and CFO. Before I get into my portion of the call, I want to turn you over to Chuck Williamson.

**Chuck Williamson - Unocal - Chairman, CEO**

Thanks, Robert, thank all of you for joining us this afternoon. I know it's been a busy day for conference calls. I will try to keep my remarks brief and try to get to questions and answers pretty quickly. I want to make a few general comments and then I'm going to turn it over to Joe Bryant who'll give you an operational update, and then Terry will talk briefly about our financial situation. As you can see from the release, we had another excellent quarter and we expect to post a strong fourth quarter. I'll say despite hurricanes, a couple of asset sales we had in Pure Resources and Brazil, and the continuing strong oil prices which have negatively impacted PSP production, we did manage to hold our production at nearly 407,000 BOE per day, which is up slightly from the second quarter. We expect the fourth quarter to be above

## UCL - Q3 2004 Unocal Earnings Conference Call

third quarter levels as a result of a full quarter of our higher Indonesia West Seno production.

Our major new production-adding projects for 2005, as we've previously outlined, remain on schedule and we certainly look forward to significant production growth from second quarter of 2005 throughout the year. Joe will briefly update you on the progress of those new projects, the Azerbaijan AIOC project, Deepwater Gulf of Mexico, Thailand Phase II oil, and the new field in Bangladesh. He'll also talk about progress we're making on what we call the next wave of development projects in Indonesia, Bangladesh and Thailand. We also have a very high degree of exploration activity in the fourth quarter and early part of next year, with high-impact wells we are going to be drilling in both deepwater Indonesia and deepwater Gulf of Mexico, as well as a very full slate of much smaller but nevertheless important tests in our North American business units.

Since the last call there's been another industry discovery in the Lower Tertiary by Chevron in the Jack prospect, which is located about 20 miles southwest of our St. Malo discovery. Joe will update you on St. Malo and La Jolla activities we're engaging in right now. We also completed the repurchase of \$150 million of common stock and redeemed about half of our outstanding preferred convertible securities, and contributed \$100 million to our U.S. pension plan.

Our balance sheet continues to improve, and Terry can update you on that in a few minutes. I think one of toughest issues we're facing is fighting rising unit costs, particularly in North America where we are not experiencing production growth. We're clearly not alone, as production services, transportation, electricity and severance taxes have all significantly increased for everyone this year. We are in the throws of budgeting right now for 2005 and are certainly addressing ways to try to reduce our expenses and flatten the unit cost. I have to say we are not ready today to provide guidance on 2005 as we're really just in beginning of that budgeting process.

But I will say that we can expect our capital spending for 2004 to be down slightly from what we had originally forecast. So we're lowering our 2004 Capex forecast from about \$2 billion to more in the range of \$1.7 to \$1.8 billion – and that's largely because we've chosen to exit the East China Sea project which we had previously budgeted for. For next year we anticipate spending, again on a very preliminary basis, but on the order of \$1.9 to \$2 billion in Capex, and again heavily dedicated to, as you can imagine, funding some of the large development projects that will be coming on line in 2005 and beyond.

We also aren't ready today to discuss our 2004 reserve ledger. We are in the midst of that process as the year concludes. But I will say that over the next year will you see us converting a lot of our PUDs to proven developed. I know there's been a lot of concern about our high PUD rate, but with these big new projects coming on that I

just mentioned, a lot of those PUDs will be converted as they come on line to produce and develop. So I think we're in a pretty good position as a general introduction in terms of entering next year. I'll now turn it over to Joe Bryant, our new President and COO, who is going to update you on some of our operations.

For those of you who haven't met Joe or didn't have a chance when we were back in New York, he's just joined us in September. He came to us from BP where he was heading the BP Angola business, so he's only been with us about one and a half months, but I can tell you he's already visited most of offices and is pretty much up to speed on most of our key operations. He is a great addition for us and I am going to let Joe update you on some of our key operations. Joe, floor is yours.

**Joe Bryant - Unocal - President, COO**

Thank you, Chuck, and nice it's to be on the call. I want to spend a few minutes talking about our West Seno product, where we are on our current development projects, the next wave of projects that Chuck mentioned, and then wrap up with a few words on current exploration. Let me start off with West Seno. If we think back to the second quarter, we were right at 20,000 barrels per day gross production in West Seno in Q2. Q3 production we were able to increase to 25,000 barrels per day, and I'm happy to say that so far in October we're averaging right at about 40,000 barrels a day. So, we've seen some very good results in the past few months that we are pretty proud of. Those results have come from some excellent horizontal wells that we've drilled, some artificial lift optimization that we've done, and workovers that we've been able to execute very well.

We've also seen outstanding drilling performance which is accelerating our drilling schedule and getting us to plateau sooner. As of today we've drilled 26 of 28 wells in the field, and as I said, are currently at about 40,000 barrels per day. So this is a big success for us and one that we're pretty proud of. I would like to say a few words about where I think we are going to go from here. We're going in uncharted territory now in the field and I think that we are going to focus our efforts right at maintaining this plateau as long as we can. I'm not able to predict how long we can remain at 40,000 barrels per day, but what I will say is that during the next several months into 2005, all of our efforts will be directed towards maintaining this plateau and then managing the decline as aggressively as we can in 2005.

Let me also say that I think the teams involved in West Seno have been through an awful lot in the last year. It's been a big struggle and I think that they have a lot to be proud of to get the field actually doubling production from Q2 to where we are today. I think for Unocal the lessons learned here have been pretty hard won, but I think they will pay enormous dividends as we execute the rest of our deepwater portfolio both in Indonesia and in the Gulf of Mexico. So we haven't lost those lessons. We'll keep them

in mind and when we continue our deepwater developments in both of those areas, we'll hopefully not make any of same mistakes again.

Let me shift gears here into the big development projects. We've talked about five big projects for Unocal. Let me just do a fly-by of those and give you some confidence on what we're thinking. In Azerbaijan, two big projects there, of course, the central Azeri project and the BTC pipeline. On Azeri, the central processing platform is set, and we are going through some conditioning work on that now. We expect to come online some time in the second quarter of next year. On the BTC pipeline, the welding is currently about 98% complete. We expect linefill to begin sometime in early 2005, and first lifting sometime in later 2005. So, on the Azerbaijan front everything is going according to plan, and we don't have any real concerns about how the next several months will play out there.

Let me jump to Bangladesh, where we are in the final stages of bringing on our Moulavi Bazar field. This is a 70 MMCFD gas plant that will go online probably around April 1. We have relatively high confidence of that date. We have relatively high confidence of the cost of that development, and I think this is an outstanding achievement especially given the record floods that they've had this year.

In Thailand, Phase II of our oil project is moving forward on schedule. We will be setting the processing platform in the second quarter of next year, and we hope to reach plateau production of 40,000 barrels a day gross by the end of the third quarter. So all is going pretty well in Thailand right now.

In the Gulf of Mexico, the Mad Dog field continues to make excellent progress. Unocal is forecasting a first oil date of about February 1 on that. We may beat that by a few days or so, or a few weeks. But for the time being we're going to hold to February 1, and things are going very well there. In addition, in the Gulf of Mexico, the K2 field is forecast for April 1 of next year and things look very good for us holding to that schedule.

So in summary, on all of these projects, we are closing in on first production with no major concerns at the present. We'll be watching the actual completion of these projects very closely as they individually and collectively have a significant impact on Unocal's 2005 production. With each passing week and month, we'll grow more confident in the startup timing and understand the wrap-up schedule for each one of these projects. As that information becomes available, we'll certainly share it with all of you.

Let me change gears here and talk about next wave of projects. It's important to say that as the construction of these five major projects draws to a close, it's imperative that we redouble our efforts on the next wave of production generating projects in our portfolio, and I'd like to say a few words about those. Let me again

start in Bangladesh with our Bibiyana field. You'll recall that this is our biggest field discovered to date in Bangladesh, with reserves estimated somewhere around 3 TCF. We are currently negotiating the final gas sales agreement in Bangladesh and we hope to have that done here in fourth quarter. We have already begun some field work that will set us up for first product in the fourth quarter of 2006. We anticipate initial production somewhere in the range of 200 to 250 million cubic feet per a day, ramping up to some 500 million three years later.

Let me jump to Indonesia deepwater and talk about Gendalo. We are in active discussions with our partners regarding a sub-sea development concept. We expect to make a final decision on the concept that we select some time in 2005. And we will expect that field to go online some time in 2007 or 2008. Again, this is Phase I of Gendalo, and we estimate production there will be about 250 to 300 million cubic feet a day when that field does come online.

Staying in Indonesia let me say a few words about Gehem and Ranggag. We are currently looking at a co-development of those two fields. We've done some appraisal work this year, and all of that has confirmed our suspicions that this would be an excellent co-development opportunity for us. We're continuing to do all of the subsurface work and some of the preliminary engineering work on that co-development. This is a very large project, and we expect that some time in 2005 we'll make selection decisions on the concept itself. We will probably sanction the project sometime in 2006, and this will be somewhat dependent on the market as that unfolds.

Staying in Indonesia, let me say a few words about Sadewa. We have just finished our appraisal drilling on that. We needed to do some work there this year to make sure we could develop the field from the shelf as opposed to deepwater. And it looks like we were able to drill the wells as we had anticipated we could. We are now doing some detailed engineering work on Sadewa that will hopefully lead us to developing that field in the 2006/2007 timeframe. Again, we hope to have something firm on that some time in 2005.

Let me move to Thailand for a moment. We've talked about the third pipeline that PTT will be developing. That timing seems to be firming up, as we understand that PTT has procured the line pipe. Now Unocal needs to focus on making the incremental volumes available, and as a reminder, that incremental line is good for about 1 BCF day. So in summary on these new projects, we are at a critical time over next few quarters. We'll be focusing on getting the front ends sub-surfaced and project engineering right, to deliver predictable operating and financial outcomes for these projects. It's great for Unocal to have such a deep stock of development options to consider as we move our resources from the current five major projects.

We'll also keep a sharp eye towards quality through choice as we make decisions on which one of these projects to put at the front of

the queue. Let me just wrap up by saying a few words about exploration and the Lower Tertiary trend in the U.S. Gulf deepwater. Let me just say a few words about St. Malo. You're aware that we drilled an appraisal well there this year. We have currently got a lot of work going on in trying to understand the data that we obtained from that well, and we expect to have most of that data back in the fourth quarter of this year. We were discussing at the same time a data exchange with about BP for an adjacent well, their Das Bump well. The outcome of that negotiation will determine the timing of our La Jolla drilling, which is adjacent to Das Bump. All I can really say is about St. Malo at this point is that there is a significant resource present.

We need to do a lot of subsurface and conceptional engineering work to understand what the development options would be and timing for those options. I'm not able to say much more at this point, and I hope that as 2005 unfolds we will have more to say. Other than that, we're currently drilling the Sequoia prospect and we hope to have that down in the next 20 to 30 days. After that we will move the Discoverer Spirit drillship to the Mad Dog Southwest Ridge well, to begin our 2005 drilling program. On the shelf, we're still building shelf inventory and monitoring industry activity. We'll continue doing that in 2005.

Back in Indonesia, we will be drilling two wells in the Tarakan Basin. We'll be able to share those results with you as soon as we can. We are also drilling some commitment wells in newly acquired PSCs. And other than that, we will continue to focus our efforts in Indonesia on monetizing the existing gas that we've already found. The last thing I'll say on exploration is that we expect to spud our Amrit Number One well in Australia, with Santos as the operator, sometime in November. So let me summarize by saying over that over the next six to nine months I think there's three things that we need to focus on. One is clearly bringing all projects on line as promised. Secondly, to make visible progress on the next wave of development projects we talked about here today. Lastly, controlling and reducing our overall cost structure and improving our operating efficiency.

This is clearly something I am spending a lot of time on. We are in the very stages here. We have a lot to do, and I hope that as 2005 unfolds we'll have a lot to talk to all of you about. So let me wrap up there. I'll be glad to answer questions later, but now I'll turn it over to Terry who will talk about our third quarter financial results.

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**Terry Dallas - Unocal - CFO, Exec. VP**

Thanks, Joe. The last time we talked, Unocal had accumulated quite a lot of cash due to operating results and also a commodity price world that was extremely attractive. Of course, that world has only become more attractive in this quarter. As you will see from our press release, we now have approximately \$800 million in cash. We did use about \$500 million last quarter, as Chuck enumerated. We bought about \$150 million of stock at an average

price of \$36.30. We contributed \$100 million to our underfunded pension plan, which brought it not quite to a completely funded position. But we certainly filled most of the gap, and we really won't know what that position is until we do most of our actuarial work. But we think we've pretty well brought it in line with where we needed to get the pension plan.

We also redeemed about half of a preferred convertible issue that we have. We used up about \$500 million to do that. With the cash balance that we see now and the cash that we're forecasting by the end of the year, we will be revisiting that balance with our Board at our next board meeting. We would anticipate that we will continue to use that cash to look at our different securities to decide what we would like to do. We have the same options that we discussed with you on our last conference call, namely buying back shares, looking at the convertible preferred which is roughly in a price range that makes it attractive to convert to common stock. And then there are other uses of the cash, but at this time I will say as a company we are comfortable with our debt ratings and ratios. We don't see any reason to strengthen our balance sheet by paying down any additional debt.

We won't be making any more statements on what we will do with that cash until we get to the end of the year and we actually know what that cash balance is. We would anticipate having that discussion and having something to talk about after the early December board meeting. With that I will turn the presentation back over to Robert Wright.

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**Robert Wright - Unocal**

Thank you, Terry. Before we get to the Q&A, I wanted to go through a few more parts of the financial performance in the third quarter and the outlook. The major elements of the financial performance in the third quarter 2004 versus the second quarter were furnished via e-mail, fax, they're posted on our website and we also furnish it to the SEC on an 8(K). This information is repeated in the last seven slides of the slide deck that I referred to earlier, slides 8-14. Unless there are questions I will not discuss those variance factors or those special items on this call.

You may of course call Investor Relations either in Sugar Land or El Segundo for more information after the call is over. I will now discuss a few other third quarter items and the latest outlook. If you will flip to slide number three, worldwide production volumes in the third quarter were approximately 407,000 BOE per day, which is up slightly from the second quarter. Increased volumes from West Seno, that Joe referred to, plus the higher volumes in Thailand resulting from higher nominations due in part to the pipeline capacity expansion, more than offset the impact of asset sales in the United States and Brazil, hurricane related production curtailment in the Gulf of Mexico and the negative impact of higher oil prices on volumes from production sharing contracts.

As mentioned in today's news release, full-year production is expected to exceed 405,000 BOE per day which is slightly above the prior outlook. Today's press release also stated our consolidated adjusted earnings outlook for the fourth quarter. You can review the major elements of that on slide number four. Since commodity prices are such an important driver of results and they've been very volatile as you can see today, I want to remind listeners that forward-looking price assumptions are subject to significant change on a daily basis and that you should look to the changes in the latest NYMEX contract prices for oil and natural gas to adjust your earnings estimates accordingly during the remainder of the year.

As shown on slide number five the outlook for non-E&P and corporate segments adjusted after-tax results in the fourth quarter and full year are as follows. The midstream marketing segment expectation is between \$18 million and \$21 million for the fourth quarter, and between \$61 million and \$64 million for the full year. Third-quarter results were impacted by a one-time non-cash charge related to the Trans-Andean pipeline amounting to \$5 million after tax. Geothermal's outlook for earnings are between \$14 and \$17 million in the fourth quarter, and between \$44 and \$47 million for the full year. The third-quarter results of Geothermal were also impacted by a one-time impact of our power operation, which was impacted by \$11 million after tax. The total Corporate and Other expected range of after-tax costs are between \$76 and \$94 million for the fourth quarter, and between \$284 and \$302 million for the full year.

The breakdown of the individual Corporate and Other segments is shown on slide number five. Our hedging program is dynamic, and volumes and prices associated with our hedges can change over time. In the third quarter the hedging program had the effect of decreasing overall revenues by \$27 million which resulted in a 9-cent per unit lower price for North America natural gas and \$1.51 per barrel for worldwide liquids. We put in place several future derivative positions that have the effect of fixed-price sales for natural gas and oil. In the fourth quarter we have fixed the price at \$5.88 for 256 million units of natural gas per day. We've also fixed the price at \$43.25 for 33,000 barrels of liquids per day. You can see that on slide six.

Hedge positions for the first two quarters of 2005 are shown on slide seven. For information on the last two quarters of 2005 and for updates to our hedge positions in the future, analysts are encouraged to check the Investor Relations section of the Unocal website for a worksheet that shows the most recent updates for monthly hedge volumes and prices. We've now reached the Q&A section of the call, operator, so please begin that process.

## QUESTION AND ANSWER

### Operator

[Operator instructions] And our first question comes from Fred Leuffer of Bear Stearns.

### Fred Leuffer - *Bear Stearns - Analyst*

A couple questions. Chuck, it seemed like a pretty positive and quick turn in West Seno. Just wondering if you could give us a little bit of color on these last six wells drilled, you know, what happened? If you've seen better productivity in the deeper zones or learned more about the reservoir, but it looks like the response has been much, much better on the last wells?

### Chuck Williamson - *Unocal - Chairman, CEO*

Yeah, Fred I'll just say on a very high level, what we've done is we completed a couple horizontal wells up in a shallower zone. I think on the last call we talked about the deeper zones being disappointing, and that really hasn't changed. So we've focused more on the shallower zones and gotten our rate up. As Joe had said, we've also done a couple of redrills and recompletions on wells that aren't being utilized, and I think we're just getting good productivity, as I said, out of those shallower zones right now. Joe, I'll see if you want to add anything to that.

### Joe Bryant - *Unocal - President, COO*

I think the operating efficiency of the plant itself is improving. We're learning how to optimize it with each passing day a little bit better.

### Fred Leuffer - *Bear Stearns - Analyst*

I know you are going to see as you go, but can you give us some idea of expected decline rates once you do top out?

### Joe Bryant - *Unocal - President, COO*

I don't want to go there. We'd like it to be as long as possible, but you know, we need to see how the field behaves on plateau now. We need to have some operating performance with wells on an individual basis, and when we have some data that we're confident in, we'll be glad to share that.

**Fred Leuffer - Bear Stearns - Analyst**

Lower 48 gas production was a little bit less than what we were looking for. It looked like maybe about half of the amount between my 450 million and your results were because of storm activity. Were there other factors, or is it just natural decline?

**Chuck Williamson - Unocal - Chairman, CEO**

Yeah, Fred, I think certainly part of it was the hurricane, as you said. There is natural decline in that, and we're simply not investing as much as you have seen in our capital budget in that. Without any intervention in any wells, natural decline is 40 percent down there, as you know, on most of the gas wells. I think our annual for the Gulf is going to look more like 15 percent or 18 percent, because we spent some capital on redrills and some deep tests and some other things. So I think what you're seeing is some natural decline, and I think we've been pretty clear that we will expect to continue to see some natural decline in the shelf assets.

**Fred Leuffer - Bear Stearns - Analyst**

All right, and lastly, any thoughts on the deep shelf program? Reviving that program?

**Joe Bryant - Unocal - President, COO**

Ask us again at the time next quarter, Fred. I believe the guys have done a lot of work on it. I am not ignoring it. We've reconstituted the group and put it under Mike Bell who has the deepwater as well. But you know, I think it's too early to the say. We will have, in the fourth quarter we have a couple of shelf wells. I wouldn't call them deep shelf. There are more step-out wells around our existing shallow water stuff.

But we're really not ready to go back exploring. Probably not until the end of '05 or even '06. I think we are waiting and watching the industry. We may sneak a well or two in there but, boy, it's not going to be a big program at this stage. I will say, Fred, it's not because we don't want to find things to drill. We are quite actively dedicating a lot of people to looking for prospects in the deep shelf right now. But we've learned our lessons from the last program and we're kind of taking a measured look at it right now. I hope we are back to drilling late next year but I can't tell you that for sure. We haven't made those decisions.

**Operator**

Thank you, our next question comes from John Herrlin from Merrill Lynch.

**John Herrlin - Merrill Lynch - Analyst**

Hi. Regarding La Jolla, you said that you're going to be sharing data with BP. Would that possibly be leading to something else, or is that premature in terms of a joint exploration there?

**Chuck Williamson - Unocal - Chairman, CEO**

What we are doing there is talking to BP about data exchange between our La Jolla prospects and their Das Bump that they are currently drilling. We're currently in those conversations with them right now, and I wouldn't think of it as a larger area-wide issue. It's really between Das Bump and La Jolla now, and we don't really have anything more to say about that.

**John Herrlin - Merrill Lynch - Analyst**

Okay, that's fine. With conceptual engineering, can you elaborate a little bit more on the kind of alternatives you're thinking about?

**Chuck Williamson - Unocal - Chairman, CEO**

Not really. This is just very, very early in the life cycle of that asset, and we're thinking about what it would take, how many wells it would take, but all very conceptually at this point until we understand what individual well flow rates could possibly be, what the reservoir would look like. All of this is very conceptual.

**John Herrlin - Merrill Lynch - Analyst**

Okay. Last one for me is Canada, you really didn't mention that much. Anything going on for the upcoming winter drilling season?

**Chuck Williamson - Unocal - Chairman, CEO**

We picked up a couple of rigs early to give us a shot at the best rigs to get started early before freeze up and we'll probably be running about three rigs earlier than we normally would this year. That's about all I can say about it.

**Operator**

Thank you. Standing by, our next question comes from Steve Enger of Petrie Parkman.

## UCL - Q3 2004 Unocal Earnings Conference Call

**Steve Enger - Petrie Parker - Analyst**

Hi, guys. A couple of things. At West Seno, obviously it's premature but based on what you've seen in the deeper zones, is there going to be some serious look at the potential for a resource downgrade?

**Chuck Williamson - Unocal - Chairman, CEO**

Yeah Steve, I think I mentioned on the last call, we will expect some downgrade, although I'll have to say I don't think it's going to be hugely material. On the last call we talked about about 10 million barrels on Phase I, because we had never fully booked it, and I still think it's in that range. We haven't finalized those numbers. And so that really hasn't changed since the last call.

**Steve Enger - Petrie Parker - Analyst**

Okay.

**Chuck Williamson - Unocal - Chairman, CEO**

Now, we haven't talked about Phase II because we've delayed Phase II in West Seno, of course, for any price revisions at the higher oil price, but in terms of absolutes, apples-and-apples for Phase I, I think we said 8 to 12 as being the range of revision. Phase II we will look at, because we are looking at an extended-reach drilling program and seeing what kind of reserves we might recover from that. I'm not ready to say what the answer to that would be.

**Steve Enger - Petrie Parker - Analyst**

You didn't have any reserves booked for Phase II, Chuck?

**Chuck Williamson - Unocal - Chairman, CEO**

I believe we had some, but it was very small. It won't be a huge number whatever it was.

**Steve Enger - Petrie Parker - Analyst**

Okay. Have you pretty well abandoned the original concept for Phase II at this point?

**Chuck Williamson - Unocal - Chairman, CEO**

Joe was just over there. I'll let him answer.

**Joe Bryant - Unocal - President, COO**

Yeah, I think we have abandoned the notion of an additional TLP out there. However, we are pretty advanced in understanding how much of those Phase II reserves we could capture with extended-reach drilling from the existing TLP. We hope to have that work done here later in the fourth quarter, and make a decision about moving forward some time in 2005.

**Steve Enger - Petrie Parker - Analyst**

Okay. Not a big deal but, Joe, you didn't mention Champlain. Does it look like that is going to go forward?

**Joe Bryant - Unocal - President, COO**

We're currently talking to our partners about that and understanding the development options that are available to us. And I can say that I think we will make a decision one way or the other here in the fourth quarter. What we know is that we're going to continue the conversations with the partners to decide where we all want to end up on that. Right now it's not at all certain that we will proceed with it. But I'm not able to say we won't proceed. I think it will play out over the next week or so.

**Steve Enger - Petrie Parker - Analyst**

We'll stay tuned. And last for me, on the Alaminos Canyon area, it's probably fairly slow-moving, but can you provide any update on discussions around the development out there?

**Joe Bryant - Unocal - President, COO**

Steve, there's really no news. We continue to be in discussions about Shell. We've talked before about a potential co-development. But I can't say any milestones have been reached, other than we continue to work on it.

**Steve Enger - Petrie Parker - Analyst**

Thanks, guys.

**Operator**

Thank you and our next question comes from Phil Pace of Credit Suisse.

**Phil Pace - Credit Suisse First Boston - Analyst**

Hi guys, how you doing?

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**Joe Bryant - Unocal - President, COO**

Good, Phil.

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**Phil Pace - Credit Suisse First Boston - Analyst**

I was just curious to know if there are plans for a production test on any of the Lower Tertiary projects, and what your next lineup of drilling in that trend is going to be?

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**Joe Bryant - Unocal - President, COO**

With respect to the production test, that is something that of course we're in initial conversations about with various operators. But there's nothing firm to talk about at this point. I think that it's in the industry's interest that we do something along those lines, but nothing's been put together yet. And your second question was, what's our drilling - ?

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**Phil Pace - Credit Suisse First Boston - Analyst**

Yeah, the schedule of the other prospects that you'd like to test in that trend from here?

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**Joe Bryant - Unocal - President, COO**

Yeah, I think that what we're doing right now is understanding how our prospect inventory matches our rig commitment next year, and making sure that we understand how we can get the most value out of the inventory versus when the rig commitment expires in September. And we're at the same time putting our 2005 plan together. So I can't really give any more detail than that, other than to say we are in active discussion on all of the above.

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**Chuck Williamson - Unocal - Chairman, CEO**

I'll add to that, Phil, I think it's just what Joe said, we recognize as a partner group at St. Malo we'll probably need to come back and drill another well. We don't know exact when, but presumably sometime next year. That has not been decided or agreed to by the partners. We've been waiting on this Das Bump trade, because I think La Jolla is high on our list in terms of "want to go drill," but as Joe said, we haven't consummated anything. I will say we have two other wells planned.

One for next year, early in the year sometime, is an extension to the Mad Dog field. We call it -- BP calls it the Mad Dog Southwest Ridge, I believe. Those of you who have followed this recognize it as a wide range of reserves carried for Mad Dog, I think 200 to 450 million barrels or thereabouts equivalent, and so the Southwest

Ridge needs to be tested and appraised. So it's really a Mad Dog appraisal well that will be drilled, Phil, probably early in the year. That's pretty much committed to.

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**Phil Pace - Credit Suisse First Boston - Analyst**

And that's a Miocene objective?

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**Chuck Williamson - Unocal - Chairman, CEO**

That's a Miocene objective. Sometime next year, we will also come back and drill -- with BP as operator -- a Mad Dog deep well in the Lower Tertiary. I'm not sure exactly when, that's BP's schedule, but my guess is in the middle of the year sometime. So we still very much like the Lower Tertiary prospectivity there beneath Mad Dog, and so does BP. We tried it last year for those of you who didn't follow it, and weren't successful mechanically.

And then another fairly significant well for us will be on a prospect called Knottyhead, in Green Canyon, which we got in a lease sale this year. We're a quarter interest holder along with Nexen and BHP and Anadarko, I believe. And so that is on the schedule pretty firm for probably sometime late first quarter or second quarter of next year. That is a Miocene.

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**Phil Pace - Credit Suisse First Boston - Analyst**

Who operates Knottyhead?

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**Chuck Williamson - Unocal - Chairman, CEO**

Well, Nexen is the operator, but we will probably drill the well for them. That's a fairly significant test for us. It was, I think, the second-highest bid block in the lease round. Amerada has the block right to the north. So, those are the two things -- the Mad Dog Southwest Ridge and Knottyhead -- that probably will appear on our schedule on the first half of the year. Mad Dog Deep later in the year. Somewhere in there, a Puma appraisal -- probably later in the year when the seismic is done. So we are putting together the schedule now. Joe is right, it's not firm exactly, but that kind of gives you a smattering of what we're thinking about.

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**Phil Pace - Credit Suisse First Boston - Analyst**

That's helpful. Thanks, Chuck.

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**Operator**

Thank you. Our next question is from Mark Gillman, of Benchmark Company

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**Mark Gillman - Benchmark Co - Analyst**

A couple things. I know, Joe, you were reluctant talk about how long you felt the West Seno plateau could last, but could I ask, have you seen any significant pressure decline or water encroachment in the first wells you brought online?

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**Joe Bryant - Unocal - President, COO**

I can't answer that.

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**Mark Gillman - Benchmark Co - Analyst**

Can't or won't?

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**Joe Bryant - Unocal - President, COO**

Can't. I just haven't had enough time to look at well data yet.

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**Chuck Williamson - Unocal - Chairman, CEO**

I can give you a little flavor, Mark. There's been one or two of the wells that have had some water encroachment, more than we expected but certainly not most of the wells. I think what we are most worried about, and why Joe is being hesitant and should be, is that we don't know about sand problems, we don't know the decline rates. We brought these wells on in the last few weeks, but we haven't had massive water encroachment, no.

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**Mark Gillman - Benchmark Co - Analyst**

Okay. Shifting to the, to the Indonesian shelf, I notice as part of your production update you were talking about production falling off there in the fourth quarter 10 to 12 percent, and I'm curious as to what that's all about and to the extent you're trying to incorporate entitlement effects there.

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**Chuck Williamson - Unocal - Chairman, CEO**

Well we just did some workovers, and so gross production was up in the third quarter. It doesn't last very long, but I think a lot of that is entitlement and is basically based on how much we've spent in the quarter and how much exploration is going on. So, as you know, I don't think it's a phenomenon of gross production. I think it's a phenomenon of entitlement and net production.

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**Mark Gillman - Benchmark Co - Analyst**

Okay. Terry, in that regard do you make a specific price forecast that underlies your production estimates that you provided in your production outlook? And if so, what is it? For the fourth quarter?

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**Robert Wright - Unocal**

Mark, it's Robert Wright. It's basically the same as it was in the third quarter. So if you have a change in the price, adjust the fourth quarter based on whatever the third quarter price was.

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**Mark Gillman - Benchmark Co - Analyst**

Okay. And if I could just shift to the Gulf of Mexico for a second, I was wondering what the shut-in volumes are currently and what you might expect for the fourth quarter?

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**Robert Wright - Unocal**

It's less than 500 barrels a day equivalent, Mark, so it's really insignificant.

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**Mark Gillman - Benchmark Co - Analyst**

Okay, that's all have. Thanks very much.

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**Operator**

Thank you. Next question comes from Albert Anton of Karl H. Forsheimer.

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**Albert Anton - Karl H Forsheimer - Analyst**

Yeah, a couple questions, one on Indonesia. I guess Bontang is still running below capacity, there's not enough gas to supply it because of natural declines mostly by Total on the shelf, and I wondering with your different projects Gendalo and Sadewa and Gehem-Ranggas, can any of these be accelerated to meet that, to fill in? I know after 2010 you'll have a greater opportunity, but can you give us a feeling for the likely gas production profile from that whole area? And my second question is on Vietnam. I will let you answers the first one first.

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**Terry Dallas - Unocal - CFO, Exec. VP**

Every operator, VICO, Unocal and Total, are working as hard as they can to accelerate gas. Every operator feels the pressure of Bontang, you know, missing cargos. There is just not a lot that can be done. Total is drilling, I think, 40 wells. Unocal is looking at

## UCL - Q3 2004 Unocal Earnings Conference Call

some major products, but they just don't look like they can be accelerated. I think, the end of 2007, 2008 is as fast as we can see that right now.

We are looking at some smaller projects that might contribute to that shortfall. Total has accelerating one of their major developments that was on the schedule several years from now and actually it's out for bid. It's scheduled some time in 2007, 2008 as well, and I know VICO's doing some small incremental acceleration projects. So everyone is working, but there is no forecast that fills the hole in the near term.

**Chuck Williamson - Unocal - Chairman, CEO**

I'll add to that, because that's one reason we rapidly appraised Sadewa in the hope that it's a two to three-year project we can get online. But it's not the size of the big deepwater project.

**Albert Anton - Karl H Forsheimer - Analyst**

Right.

**Chuck Williamson - Unocal - Chairman, CEO**

We're trying, just like Terry said, I think every operator is trying very hard to make up four some of those last cargos.

**Joe Bryant - Unocal - President, COO**

Yeah, let me jump in as well. I think it's important to understand what the critical path item is on these projects, and that's what we are doing right now. We have to answer that before we can really have a conversation about accelerating them. But I think that probably the critical path is going to be pipeline equipment in deepwater, and of course, we all know what's going on in deepwater around the world right now that's competing for the same equipment. So as we can get more visibility on how we can access equipment there is some possibility of accelerating this, but I wouldn't put it at a very high percentage.

**Albert Anton - Karl H Forsheimer - Analyst**

I understand. On Vietnam, you have a memorandum of understanding with the government. They apparently are pretty short on power, electrical outages and so forth. You have pretty substantial potential reserves there, and I wonder what the timing looks like out there?

**Chuck Williamson - Unocal - Chairman, CEO**

We've found the gas, and we've appraised a lot of the gas. What we're doing now is working with the government, because the government needs to get financing for the onshore infrastructure, the power plants, basically. And so that is a critical path item. They have gotten financing I think for two of the 300-megawatt plants, but they have a ways to go. And so what we have said is that publicly, we are trying to be able to deliver gas by 2008 or 2010. But the reality is we are not going to sign any gas agreement until they have the infrastructure in place.

So, you know, I can't give you more timing than that, but it's nothing real short term. They definitely need the gas and they need the power generation, but they also have to be able to afford the infrastructure for it. So we are basically done drilling in Vietnam. We are now working with the government and EBN to see if we can come up with a suitable power development feasibility plan.

**Operator**

Our next question comes from, Gil Yang, Smith Barney.

**Gil Yang - Smith Barney - Analyst**

Hi, most of my questions have been answered. But I was just wondering if in your planning for St. Malo, if you've factored in the higher steel cost that we're seeing these days into your development ideas?

**Joe Bryant - Unocal - President, COO**

Yeah, this is Joe. I don't really have an answer for that. We're so conceptual in St. Malo that we wouldn't have any idea what impact steel itself would have on the development. There will be a time when we can get that granular, but we certainly don't have that data today.

**Gil Yang - Smith Barney - Analyst**

Okay, so it's just too early to talk about that.

**Joe Bryant - Unocal - President, COO**

Absolutely, yeah.

**Gil Yang - Smith Barney - Analyst**

Can you talk about the five big projects that you mentioned earlier on in your comments? Are there reserves still to be booked as you

## UCL - Q3 2004 Unocal Earnings Conference Call

bring those projects on line, or they have already been they fully booked?

**Chuck Williamson - Unocal - Chairman, CEO**

Let me take a shot at it. In Azerbaijan, we'll start with Azerbaijan, this year we sanctioned Phase III, and we will be adding those reserves to our books, and then we'll be pretty fully booked for the field. That'll be a reserve add in this year.

**Gil Yang - Smith Barney - Analyst**

Can you quantify that?

**Chuck Williamson - Unocal - Chairman, CEO**

I can't quantify it because I don't have the number in front of me, but the other thing to remember in Azerbaijan is the higher oil price will lower our existing reserve number on a PSC revision. So we'll be adding new reserves, but we'll probably take some off as long as oil prices stay high through the end of the year. But we will separate the the price effect. The other projects, K2 and Mad Dog in the Gulf of Mexico, are very small. We've booked part of them. We will wait until we get the wells on production next year and see performance before we make any major changes in reserves there. They'd be small changes if we make any this year.

Bangladesh, we have booked Moulavi Bazar, the new field that's coming on in 2005. We hope to have a new gas sales agreement for Bibiyana within this next quarter, and we would book those reserves for the twenty-year life of the gas contract as Joe described in his earlier comments. And then finally, the Thai oil project. I think we booked part of that. It won't be a huge addition, but there'll probably be some additional adds. But most of that will come after we have the wells on performance and, we see how they are going to deplete or not deplete. So the big pieces for us this year on those five new projects are going to be Azerbaijan Phase III, offset by some price revisions, and then if we sign the gas sales agreement which we expect in the fourth quarter for Bangladesh.

**Gil Yang - Smith Barney - Analyst**

Okay. That you.

**Operator**

Thank you. Our next question comes from Phil Pace of Credit Suisse.

**Phil Pace - Credit Suisse First Boston - Analyst**

Just a follow-up for Terry. It kind of slipped in there that there was a couple hundred million dollar reduction in your '04 capital budget, which seemed like a really big number. Could you talk about what other items affected that, and how much of that was the East China Sea operations?

**Terry Dallas - Unocal - CFO, Exec. VP**

The East China Sea operations was well over \$100 million of it. We also announced earlier that Phase II of West Seno was delayed, that was tens of millions. So those were by far the two biggest pieces, and then there were odds and ends that made up the rest. And we did invest a little bit more than we had budgeted in mostly onshore U.S., in Pure. We've been doing some additional work there. But the biggest piece in terms of reduction is by far China, and then second, the Indonesian investments.

**Chuck Williamson - Unocal - Chairman, CEO**

Phil, on the China project, the reason that number is so big is that we had an option to basically pay for some costs that we had budgeted over \$100 million, for that option to be exercised, was \$140 or \$150 million I think.

**Phil Pace - Credit Suisse First Boston - Analyst**

And why did you end up walking from that project?

**Chuck Williamson - Unocal - Chairman, CEO**

It's a long story, but the short version is pretty simple. We and Shell both walked, after a lot of effort to get there, simply because we couldn't commercially get to the terms that made it attractive for us. And that's the simplest way I can put it.

**Phil Pace - Credit Suisse First Boston - Analyst**

That's fair. Thank you, guys.

**Operator**

Thank you. And our next question comes from Rehan Rashid from FBR.

**Rehan Rashid - FBR - Analyst**

Most of my questions have been answered, but just a broader thought, a lot of development projects are coming online in the

## UCL - Q3 2004 Unocal Earnings Conference Call

next several quarters. On the exploration front, any thoughts on deepening the portfolio? Or do you guys feel you've got enough going on from an exploration standpoint to run with things the next few quarters?

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**Chuck Williamson - Unocal - Chairman, CEO**

Yeah, I think it's a very good question. It's something we are very, very much interested in working on right now. We certainly have plenty of exploration inventory for the next, I think, couple of years in the Gulf of Mexico, because there's been some new plays opened up and we have a very big acreage position there. And not just in the Lower Tertiary, but a couple other trends. In deepwater Indonesia, we know that will play out, but we have three new large PSCs that only have one well drilled on them.

We are drilling a well on one right now, in fact, so we still have exploration running room there. But I tell you, we are constantly looking, particularly around Asia, for new opportunities for exploration farm-ins or other ways to replenish our portfolio. I don't think we are, at least I'm not, satisfied at this point that we have enough for the next five years, no. I think we will need to replenish that, but we have a couple of years to do that. And we're working on it very hard right now.

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**Operator**

Thank you. Our next question comes from Michael Prince, Blue Star Industries.

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**Michael Prince - Blue Star Industries - Analyst**

Chuck, Terry, Robert, what a great quarter. I can remember when that wasn't done for the year. So congratulations.

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**Chuck Williamson - Unocal - Chairman, CEO**

We appreciate it.

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**Michael Prince - Blue Star Industries - Analyst**

Yes. Chuck, I guess I'll direct this at you. In the Gulf, what would it take – or is it ever going to be – that we are going to be back in Ship Shoal, Eugene Island, South Marsh, or Vermillion? Is that ever going to happen again? Would it take \$80 dollar oil or \$12 gas, or is this just played out now?

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**Chuck Williamson - Unocal - Chairman, CEO**

You know, it's a tough question. But I gotta tell you, we are still in those places. Ship Shoal 208 is one of our bigger fields. But it is, I

harder and harder to find the drilling opportunities to make large investment there. And that's even at \$50 dollar oil and \$6, \$7 gas. So I can't tell you that I think the future's that bright for some of those older areas. But we continue to have some small success, deepening some of the fields wells, doing step-outs, doing down-dip tests, et cetera, that are very good money makers for us, and frankly, they allow us to keep our decline to 15 or 20 percent, rather than 40 percent. So we continue to invest in those. But I would be fooling anyone to think that, particularly the inshore areas, have huge remaining potential left. Most of it is fairly small stuff and incremental to your infrastructure.

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**Michael Prince - Blue Star Industries - Analyst**

I was under the impression with the higher commodity prices that it may be worth your while, but obviously it's not, I guess.

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**Chuck Williamson - Unocal - Chairman, CEO**

We encourage our guys to present those opportunities to us because, you know, in the short term they can make a lot of money. But you also have to have resources with the them.

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**Michael Prince - Blue Star Industries - Analyst**

Very good. Again, congratulations, terrific quarter.

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**Chuck Williamson - Unocal - Chairman, CEO**

Thanks.

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**Joe Bryant - Unocal - President, COO**

Thanks, Mike.

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**Operator**

Thank you, and at this time I would like to turn the meeting back over to Mr. Wright for any closing remarks or final comments.

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**Robert Wright - Unocal**

Thanks, everybody. It's coming up on two o'clock here, which is real late wherever you are. And thanks for participating in the call. I know it's been a long day and we appreciate your patience. This concludes the third quarter conference call. Thank you.

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