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SU.TO - Q1 2017 Suncor Energy Inc Earnings Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Suncor's First Quarter 2017 Financial Results Call and Webcast.

I would now like to turn the call over to Mr. Steve Douglas, Vice President, Investor Relations. Mr. Douglas, please go ahead.

Steve Douglas *- Suncor Energy Inc. - VP of IR*

Well, thanks, Drew, and good morning, everyone. Welcome to the Suncor Energy First Quarter Earnings Call. I have with me here in Calgary, Steve Williams, our President and Chief Executive Officer; along with Alister Cowan, Executive Vice President and Chief Financial Officer.

I'd ask you to note that today's comments do contain forward-looking information, and actual results may differ materially from expected results because of various risk factors and assumptions, and those are described in our Q1 earnings release as well as our current AIF, and these are both available on SEDAR, EDGAR and our website, suncor.com.

There are certain financial measures referred to in these comments that are not prescribed by Canadian GAAP, and for a description of these, please see our first quarter earnings release.

After our formal remarks, we will open the call to questions. First, from members of the investment community, and then, if time permits, members of the media.

With that, I'll hand over to Steve Williams for his comments.

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Good morning, and thank you for joining us. Gosh, what a difference a year makes. In the first quarter of 2016, crude prices averaged less than $35 a barrel. And I think the term that we've used a lot now, lower for longer, was in common use then. And many in the industry were fighting to survive.

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Since that time, crude prices have risen by well over 50%, but still around $50 per barrel. Investment has began to ramp back up and there's considerably more optimism across the industry.

However, one thing that hasn't changed in the past year is Suncor's focus on operational excellence and capital discipline. We began our efforts to improve reliability, drive down operating costs and lived within our means long before oil prices fell. And we intend to continue those efforts, regardless of the business environment going forward.

In the first quarter of this year, we continued to make significant progress. Our Oil Sands operations had one of its best quarters ever. Mining In Situ and Upgrading all ran well over 90% utilization rates, and costs continued to decline.

Our Oil Sands costs were just at CAD 22.55 per barrel, and remember, that's Canadian dollars. So in U.S. dollars terms, that's less than $17 per barrel. So our cash costs were 7% lower than the same quarter last year, and this was achieved while absorbing a 46% increase in natural gas costs over the year.

At Syncrude, we were disappointed to have operations interrupted by an unplanned outage in mid-March. In the last quarterly call, I cautioned that it would be premature to expect the elevated level of performance we experienced at Syncrude to continue over the coming quarters.

We know that the journey to operational excellence is never a simple straight line, and that's why we set 2020 as the target year to achieve sustainable utilization rates of 90% and cash costs of $30 per barrel or less. And I'm still convinced that these goals are achievable and that Syncrude is on the path to operational excellence.

In fact, we're moving forward at pace on the Syncrude performance improvement initiatives, and we're actually seeing more synergy opportunities today than when we increased our working interest about a year ago.

Turning to E&P, I'm particularly pleased with the performance of our offshore projects. Reliable operations, reservoir optimization initiatives and new wells coming online resulted in production significantly above forecast for the first quarter, and lifting costs were less than $5 per barrel in the North Sea and less than $10 per barrel on the East Coast of Canada.

Because of this strong performance, we've been able to raise our E&P production guidance, which offsets the reduced production at Syncrude. The net result is no change to our overall production guidance for the year.

In the downstream, Refining and Marketing business turned in another excellent quarter, despite slightly weaker gasoline demand. Our refineries ran at 93% and took advantage of improved distillate demand and stronger wholesale and reached the margins.

Our integrated model ensures consistent cash flow generation, regardless of crude price differentials.

Approximately 85% of our bitumen production is either upgraded at our base plant for Syncrude or it is processed through our refineries. And this makes us very resilient to light-heavy differentials. A widening or narrowing of the price differential has almost no impact on our cash flow as we capture the benefits of the full value chain. And of course, that cash flow has led the industry on a per barrel basis for the past several years, with the first quarter continuing the trend of reliable, low-cost and highly cash-generative operations.

Looking forward, the Syncrude outage combined with planned maintenance at Firebag and the Number 2 Upgrader will reduce production in the second quarter. We're sufficiently confident in the performance of our upstream assets that we've maintained overall production guidance for the year. And we fully expect to be within the original forecasted range of 680,000 to 720,000 barrels per day for 2017.

If we achieve the midpoint of guidance this year, that will represent a year-over-year increase in production of more than 12%.

With Fort Hills and Hebron expected to achieve first oil by year-end and ramp up through 2018, we anticipate production growth of over 10% again next year.

Speaking of Fort Hills and Hebron, both projects are tracking according to plan. At Fort Hills, construction reached 83% complete as of the end of the first quarter, and 26% of the plant is already in the hands of operations, including the mine, ore preparation, hydro transport and primary extraction. With peak construction activity now safely behind us, we are on track to meet the budget and schedule we laid out on our past call.

At Hebron, the platform is now complete and awaiting an appropriate weather window to be towed back to the field location and begin drilling activities. The project remains on track to produce first oil by the year-end.

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So our major growth projects are rapidly moving towards completion. And we will soon start to see the benefits of continuing

(technical difficulty)

through the downturn in oil prices.

With oil prices gradually recovering, we've recently seen a couple of large transactions. We've continued the consolidation of Oil Sands that of course Suncor began over a year ago. This is a development that we foresaw several years ago when we first -- I'm talking about the concept of natural a oil sands developer. We recognize that resource could be more efficiently and effectively developed by companies, whose core business was oil sands. We saw the potential to better leverage infrastructure, reduce costs and improve productivity. So we view this as a very positive for the industry, the province and the country.

The Oil Sands business needs focused operators with a strong balance sheets and deep expertise, and we expect the transition to more concentrated oil sands leaders to enable regional synergies and technology development that will drive the sector forward and ensure its global competitiveness in decades to come.

We continue to evaluate opportunities for further consolidation in the Oil Sands, but we set a very high bar in terms of our returns. And given our portfolio of development opportunities, and the fact that we now hold a majority working interest in both Fort Hills and Syncrude, we do not feel any pressure to pull the trigger on another oil sands acquisition.

Our next key development opportunity in the Oil Sands is In Situ replication. We were very pleased to learn in March that the Meadow Creek East project, representing the first 2 phases in Suncor's In Situ replication program, have received regulatory approval. This is the first large-scale approval piloted and issued under the Alberta Energy Regulator's emerging Integrated Decision Approach. And it is Suncor's first (inaudible) project approved since Firebag in 2001.

So this full life-cycle approval of Meadow Creek encompasses what previously would have been hundreds of individual approvals and over a decade-long process. So this is an important foundation for Suncor's organic growth program that puts us at approximately 400,000 barrels a day of In Situ production through 2020.

Finally, I wanted to take a minute to acknowledge another recent Suncor announcement. This week, we initiated a $2 billion share buyback program. As I mentioned on the last call, with our capital spending expected to decline approximately $1 billion this year, and average oil prices trending higher year-over-year, we are well positioned to significantly grow our earnings and generate strong free cash flow for our shareholders.

We believe that share buybacks are an efficient means of returning a portion of that free cash back to our shareholders, particularly at current share price levels.

So when combined with our recent 10% dividend increase, I hope this demonstrates our commitment to increasing shareholder returns as production and free cash flow grow over the next few years.

So to go into a little more detail on that free cash flow and the rest of our financial performance, I'll hand over to our Chief Financial Officer, Alister Cowan.

Alister Cowan *- Suncor Energy Inc. - CFO and EVP*

Thanks, Steve. In the first quarter, our benchmark crude prices have reached more than $50 per barrel for the first time since mid-2015. We realized improved pricing across our system and we were able to post strong financials once again.

In the first quarter, we generated just over $2 billion in funds from operations and $812 million in operating earnings. The funds flow number is particularly notable, given that Q1 cash flow has reduced by approximately $400 million due to the annual share-based compensation payouts and the seasonality of statutory benefit payments.

Our funds from operations in the quarter more than covered our total capital spending of $1.4 billion and our dividend of $574 million.

Now even with the prices recovering slightly, we maintained a rigorous focus on cost management right across the company. Our total operating, selling and general expenses declined by 2% versus the first quarter of 2016; at the same time that our total production increased by almost 5%. This reflects our continued effort to sustainably take costs out of the entire business.

Now Steve mentioned earlier our blended Oil Sands cash costs fell to $22.55 per barrel. And this continues the trend that has seen us reduce Oil Sands cash costs by over 40% in the past 5 years.

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In the Offshore business, total expenses were down over 30% quarter-over-quarter, thanks to lower logistics costs, improved workforce productivity and a general focus on cost management. When combined with strong production, we achieved operating costs $9.75 per barrel on the East Coast and just $3.75 per barrel in the North Sea.

On the capital front, we invested $1.2 billion in Q1, putting us right on track to meet our guidance for the year of $4.8 billion to $5.2 billion. And of course, as Steve said, that represents a reduction approximately $1 billion from last year's capital spend.

Our strong balance sheet was a strategic asset during the downturn, and it remains equally important as prices recover. We finished the first quarter with approximately $3.6 billion in cash, a net debt to cash flow of 1.0x, and debt to capitalization of 27%.

With approximately $7 billion of unutilized lines of credit, we have ample liquidity, particularly given the improving crude price environment.

This past week, we took steps to further strengthen the balance sheet through the early redemption of $1.25 billion in long-term debt, and this will reduce our total debt to capitalization to the middle of our target range.

With an even stronger balance sheet and free cash flow being generated, I'm very comfortable launching into share buybacks again in addition to the February dividend increase of 10% per share.

But subject to market conditions, we expect to execute aggressively on the buyback program in the months ahead, in keeping with our commitment to return cash to shareholders.

Looking forward, you should expect no surprises with Suncor. We will continue to invest prudently to grow our core business. We'll continue to reduce costs across the entire enterprise to ensure that our business is sustainable and we'll cover our dividend at a USD 40 per barrel oil price. We'll continue to treat the balance sheet as a strategic asset that enables us to take advantage of opportunities as they arise and we'll continue to focus on returning an increasing amount of cash to our shareholders as our production and cash flow grow.

With that, I'll pass it back to Steve Douglas.

Steve Douglas - ***Suncor Energy Inc. - VP of IR***

Well thank you, Alister and Steve. Just a couple of notes before we open to mics. Crude rose modestly in the first quarter versus the fourth quarter of '16, so we did have a FIFO gain after tax of $43 million.

Stock-based compensation was a net after-tax expense of $72 million. And with a modestly rising Canadian dollar in the first quarter, we had an after-tax gain of $103 million from the impact of exchange rates with the U.S. dollars.

(technical difficulty)

due to strong performance and a continued strong outlook, our E&P production range has been

(technical difficulty)

offsets the decrease of 15,000 barrels per day in the Syncrude production range as a result of the incident at Syncrude in the second quarter -- or in the first quarter, rather.

Syncrude cash costs, as a result of that, have also been adjusted. The new range is $36 to $39 per barrel, and the royalty rates have been increased to 3% to 6%, reflecting a move from gross to net royalty calculation.

With that, I'll turn it back to the operator for questions.

QUESTION AND ANSWER

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Operator

(Operator Instructions) And our first question comes from Benny Wong from Morgan Stanley.

Benny Wong - ***Morgan Stanley, Research Division - VP***

Just looking at your overall op costs at Syncrude, it seems to -- you expect it to be at a relatively flat level on an absolute basis despite the outage. Is this because the repairs are not expected to cost very much? Or is there something that is being done there to kind of mitigate any additional repair costs?

Steven W. Williams - ***Suncor Energy Inc. - CEO, President and Non Independent Director***

Thanks, Benny. I mean, a few things there. I mean, overall we have a program at Syncrude similar to Suncor in terms of the constantly working on improving reliability, reducing costs. So we're very comfortable that, that continues. In terms of the repair costs at Syncrude, they will be relatively minimal net to Suncor because of our -- we're covered by insurance. So it's a very small number, as you've noted.

Benny Wong - ***Morgan Stanley, Research Division - VP***

Got it. Understood. And are there any lessons learned from the Syncrude outage that you'd be able to share? And going forward, what options or tools might be available to you guys in another situation like this, that you might start realizing as you're looking at the synergies you're talking about?

Steven W. Williams - ***Suncor Energy Inc. - CEO, President and Non Independent Director***

Yes, two or three things I would say. First, in terms of the event itself. I think, I've certainly had a number of questions about, hey, Steve, was this because you guys were running this plant hard? And I can say completely, unambiguously, absolutely no connection. This incident was not on one of the upgraders. It was on one of the -- on the naphtha hydrotreater, and it was what we call a freeze-thaw split in a 6-inch pipeline there, where during the winter, where the piece dissolved, this particular line was a recycle line that is not used very often, had frozen and sort of stayed okay then during the cold of the winter. As the warming season comes, then the ice plug that's been in there which has caused some damage relaxes, thaws and then you get -- the leak occur. So this is disconnected from the way we've been operating the plant, which is a small piece of good news in there. So this is a one-off event that we don't expect to see translate into future unreliability. I think your question though was more around how can we -- are there things we can do in terms of connectivity, how we can operate? And it's probably just worth me saying a few things that I think have not been very clear. The first one is we never shut Syncrude down. We actually kept one of the upgraders operating, and it's still operating now. We've been operating it at minimum. It makes the start-up of that train much easier as we put the hydrotreaters onto the back of it. So we're in a good position for the start-up. I expect the first train to be up within the next week, and really all we're having to do is start the hydrotreaters up and then link them up to the upgrader. So you can expect us to, through the coming weeks, ramp the first unit up. And then the second one, which we took the opportunity to go into turnaround on, we'll see the other upgraders come up and steadily ramp up through June as we come back from turnaround. So the situation is a little bit different than I think has been widely perceived. And one of the reasons for that was because for the first time, we actually took intermediate products and put them into other refineries and other upgraders. So what that meant was we were able to keep that. We would have hit -- tanked talks on Syncrude had we not done that. But by thinking differently, for the first time in its 40 years, we were able to export those intermediate materials. That's exactly the sort of synergy we've been talking about in the past. In this case, we've been able to do it with 2 intermediate products, a naphtha stream and a gas oil stream. Now if I go into the -- the other question I've been getting is, so how does this relate to the whole improvement program for Syncrude? It's been moving at pace. So we have complete alignment between the owners now, Suncor, Imperial and the minority owners, to move ahead with an accelerated program to look at all of the synergy opportunities. That project is going very well. We will come out with more detail on each of them, but we have 70 pieces of work, projects which are part of that overall initiative. We're excited by it. I mean, what it's telling us is the synergies are bigger than we expected, and we'll be moving ahead a little bit faster than we planned. So things are looking good in terms of the overall connectivity and synergies.

Benny Wong - ***Morgan Stanley, Research Division - VP***

That's great color, Steve. And just as my final question, as we're looking at Fort Hills as it approaches completion later this year, how do you guys think about marketing the product? Do you already have customers in place that are willing to take those barrels? And any risk that it would take some time for those barrels to be accepted? I'm just wondering if the paraffinic froth treatment makes any difference in terms of how the refiners perceive the product.

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Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Well, I mean, a few comments. First of all, just generally in terms of Suncor's growth, the industry growth, I mean, clearly our strategy was to work on the climate change (inaudible) with levels of government to get market access clearly planned and supported. And that program has been very successful. By working in a different way with our regulators, with our levels of government and with the NGOs, we now have 3 pipelines. We have Keystone, we have Line 3 and the Trans Mountain pipeline. So market access, much better position. And Fort Hills per se wasn't depending on it, but the general industry health and growth was. So I'm pleased with that progress. It's a big step forward. In terms of the product itself, it is a product which sells at a premium. So it's a high-quality product. We have been working with the market, and we're comfortable that we won't have an issue marketing it.

Operator

And our next question comes from Guy Baber from Simmons & Company.

Guy Allen Baber *- Simmons & Company International, Research Division - Principal and Senior Research Analyst, Major Oils*

Sticking with the Syncrude theme here a little bit, have you been able to go back and quantify what you think the opportunity costs with respect to lost cash flow associated with the downtime from Syncrude relative to the plant entering the year?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Well, I mean, of course -- I mean, we are in the process of doing that. It's a little bit premature to come out with a number, but we'll be clearer as we start to wind the event up. But of course, for Suncor we haven't changed our guidance. So the actual impact has been fairly well mitigated. Clearly, we refer it not to happen. But if you look at the fact we've been able to keep one of the upgraders going, a lot of that product was in tankage and we'll eventually be hydrotreating coming to market. If you look at the fact we were able to take the turnaround, which was planned turnaround anyway, that we were able to mitigate it with that. So -- and we've got an E&P business which has done extremely well. So from a Suncor cash flow point of view, some more product from E&P, less from Syncrude, slightly higher across at the Syncrude plant. But overall, we've been able to largely mitigate that impact through the steps we've taken. Now we've used the opportunity costs, of course, as the driving force to make sure that the reliability of that plant is improved. And so we'll be quantifying that and using it to focus our priorities or in making sure that event can't happen again.

Guy Allen Baber *- Simmons & Company International, Research Division - Principal and Senior Research Analyst, Major Oils*

Great. That's helpful. And then can you talk about -- I wanted to talk about the buyback a little bit. Can you talk about the thought process behind the decision to size the buyback at $2 billion over the next 12 months? How did you come to that decision? And then I would think it appears pretty obvious that the free cash generation is only going to improve as we move through this year and into 2018 as production grows, as CapEx continues to decline or declines post completion of these projects. At what point do you all have to consider extending or even upsizing that program? So just some clarity with -- or some color with respect to how you're thinking about that would be helpful.

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Okay, yes. I mean, and I'll do it at the sort of helicopter level, and then if Alister wants to jump in, he will. I mean, first of all, I hope what you've seen over the last 5, 8 years now, is a rigorous capital discipline. So we look dispassionately at the uses of our shareholders' capital, and we look at the organic opportunities, we look at the inorganic opportunities, and we look at returning it through dividend and share buyback. You've seen us continue to move dividends as we've grown the production of the company, and you will see that continue into the future. You've seen us -- and we're finishing 2 of the biggest projects in Canadian industry are coming to fruition in this next year. So you've seen us, where appropriate, start and then finish major organic capital investments. And you've seen us, we've started this consolidation of the industry a year ago with Canadian Oil Sands and Murphy. You've seen us prepare to the -- we view those deals to be of very high value. You'll see us do deals there. So you've seen that we are open to all of the potential uses of capital. Our view at the moment is, given the way we have restructured the company, given the assets we now have in the company -- and when we look at those 3 opportunities available to us, organic investment, we've got a long list of excellent projects and we will look to trigger those. I don't see those being triggered in the next year or 2. I think we're further back in terms of triggering the next generation of In Situ replication in the early -- for the early [20s]. But there's considerable investment, 400,000 barrels a day plus of capacity there. We've got some minor -- I call it minor in terms of investment, but significant in terms of potential production opportunities for debottlenecks with the new assets that come on. So with Fort Hills and with Syncrude in our portfolio,

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we've got some good low-cost, high-return projects there. So that's great. We've looked at the M&A opportunity. We've got the first mover advantage, we believe, with the Syncrude deal. I said that I believe the window was shutting. And for Suncor, because of our rigorous focus on value, that window is -- was and is starting to close. And we're seeing that. The success of deals are good -- kind of good deals but they are more expensive than the Canadian Oil Sands deal. So given that world and our view of the future, we view that having those dividend, our next opportunity is share buybacks. And these share prices, we're very happy with that investment. So Alister used a word, and it was carefully picked, it's a relatively aggressive share buyback. We intend to -- everything else being equal, we intend to go ahead and execute this share buyback in the [12 months].

Alister Cowan *- Suncor Energy Inc. - CFO and EVP*

Yes, Steve, I was just going to emphasize to everybody on the call that come May 2, we will be in the market buying our stock back. This is not just an announcement. It's an actual intent to buy our stock back.

Operator

And our next question comes from Neil Mehta from Goldman Sachs.

Neil Singhvi Mehta *- Goldman Sachs Group Inc., Research Division - VP and Integrated Oil and Refining Analyst*

A quick question for you on the E&P segment, clearly outperforming our expectations in the guidance that you set out a couple of months ago. Can you talk about where the source of surprise has been at the E&P business?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Yes, thanks, Neil. I mean, it's a fairly simple answer, Neil, to be honest. I mean if you think of the new wells we've been drilling at Hibernia, Buzzard has come off its turnaround, operating very well. So it's real fundamentals in the business. So it's good because it's not -- it's a very good indicator for the future as well. Not necessarily at exactly these levels, but very encouraging. And the selective investments we made on the new wells has gone well at Hibernia, turnaround has gone extremely well at Buzzard. And so it's a very encouraging trend.

Neil Singhvi Mehta *- Goldman Sachs Group Inc., Research Division - VP and Integrated Oil and Refining Analyst*

That's great. And as a follow-up on the buyback question, often, energy companies announce large share buyback authorizations, but in terms of execution, history would suggest that the sector tends to fall short of authorizations. So I want to be clear, the $2 billion number is not just an authorization in your view, but at a let's call it a $50 oil price flat to the curve where we are, it's your expectation that you execute this program to the entirety of the authorization over that time?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

I mean, not only would I say, yes you've got it right there, but just judge us by our track record. We bought $5 billion of our stock back through our last sequence of programs. So when we commit to them, I would have to say, not withstanding something else that we're not foreseeing at the moment, but our plan is to execute on that program. In fact, I sort of portrayed in a way the Canadian Oil Sands acquisition as we had effectively pre-bought it by buying our stock back through the previous 3 years.

Neil Singhvi Mehta *- Goldman Sachs Group Inc., Research Division - VP and Integrated Oil and Refining Analyst*

Great. Last question for me is on refining. Just Steve, where do you think we are in terms of the Canadian refining cycle? It's always tricky for us to get good pricing views in terms of Canada, but your business held in better than a number of the merchant refiners we cover here in the U.S. last year. Can you just talk about that outlook in '17?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

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Again, I would say you're right. I mean, the -- first of all, let me come back to the general mix of upstream and downstream. We're in a very good position. The net effect of the Syncrude increased ownership was -- if you look at a combination of the balance of upgrading and refining to our upstream, we're in exactly the spot we like to be, which makes us almost indifferent to the differentials that others is subject to. So we like the position we're in. We think those refineries are -- kudos to the downstream team. They are run extremely well. We're able to capture those margins. And I think when we sort of made the point a few years ago that we believe -- not that we're impervious to market, we all have to be subject to the market effects, but we were able to mitigate much more than most. So that we tend to operate very well financially at downstream through the cycle relative to others. And we are -- as you say, we're the #1 downstream operation on this continent now, and have been for a number of years. So we tend to be relatively robust even though we've seen -- we saw some -- the first quarter was viewed to be, in some ways, a difficult quarter when we look to that 3, 6 months ago. But we've been able to operate very effectively through it. So I'm very encouraged and I think it is a sign of what you can expect in the future.

Operator

And our next question comes from Paul Sankey from Suncor (sic) [Wolfe].

Paul Benedict Sankey *- Wolfe Research, LLC - MD and Senior Oil and Gas Analyst*

Steve, this question is I think about as good as you're going to make it. I was wondering, what does the Canadian dollar, U.S. dollar exchange rate mean to you in terms of actual impacts but also in terms of how you're looking at future planning?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Okay. And again, Alister will pick the question up. But just to say, I mean, another factor of the construct of the way we -- the balance of products we have, the way we move them and the fact that crude is a U.S. dollar-based price means that we're relatively robust through exchange rate changes.

Alister Cowan *- Suncor Energy Inc. - CFO and EVP*

Yes, just maybe some numbers with the sensitivities to the underlying. About $1 move in the reduction in the Canadian dollar -- or a $0.01 move, sorry, in the Canadian dollar is about $130 million extra cash flow for us. On an earnings basis, a bit flat given the translation impact on the debt. But cash flow would increase by about $135 million.

Paul Benedict Sankey *- Wolfe Research, LLC - MD and Senior Oil and Gas Analyst*

Yes, great. And Steve, then, a totally separate subject, you guys are differentiated by being the ones that did the deal at the bottom. As you look from your point of view, is the bottom of the cycle behind us and the M&A market now tend to be less attractive?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Certainly. I would like to be very reflective and critical of the actions we take. So we did go back and take a very close look and asked ourselves, with everything you've got, with all the information you have now and with the benefit of hindsight, would we have done something different? And we believe we've got it right. We believe we got that deal at the bottom of the market. Of course, as you would expect, we had the opportunity to look at the subsequent deals as well and you can tell what conclusion we came to. The only thing I would say is we are -- the core of Suncor's business is Oil Sands. There are known sellers out there. If you look, the exodus from oil sands by a lot of the big international companies I don't think is quite finished yet. And so there may be some incredible opportunities because I don't think there are many companies out there now with a balance sheet capable of purchase. So we have no plans or intentions. That's clear. We've committed to our share buyback. But I have a feeling that there may be a bit of a double bottom there, that you may see some of these come back around again.

Paul Benedict Sankey *- Wolfe Research, LLC - MD and Senior Oil and Gas Analyst*

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Yes, it does seem that the exit -- the notable exit that you referred to there from the sort of mega international majors is more opportunistic than thematic. Would you agree with that?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

No -- I agree. I mean, I think the -- I mean, you have to talk to them about why they are exiting, but I think that's for reasons of strategy to do with their corporations. What it means is, as you say, there are just potentially some growth opportunities coming along. But just look at our track record. We are opportunistic. We're a value buyer, and we only buy -- we absolutely -- if it's a great deal. And we feel no pressure. We've got 12% growth, 10% growth, and then we've got 400,000, 500,000 barrels a day of organic growth opportunities after that. So it's the perfect position to be in, and we feel no pressure to be engaged in acquisitions going forward.

Operator

Our next question comes from Roger Read from Wells Fargo.

Roger D. Read *- Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

I guess a question at this point, you talked about earlier debottlenecking the Fort Hills and Syncrude as you go forward. And I believe in the presentation the indication was Fort Hills' upfront cost was about 83,000 per flowing barrel. Can you give us an idea of the debottlenecking kind of CapEx that may occur? Or if you don't even want to think about it that way, just sort of the cost going forward on a per barrel basis for some of that growth as you work through these 2 big projects.

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

Okay. I mean, it's a little bit early to be absolutely specific about Fort Hills and the costs there. But what I would do is just reference you back to -- I remember, gosh, it must be 4 years ago now, we came out to the market and said we've got some debottlenecking opportunities and we had exactly this conversation. And we talked back then about 100,000 barrels a day of potential opportunities through a mix of debottlenecking, improving reliability, these operationally excellent type investments. And the net result of all of that was, if you look at 100,000 barrels, then the very low --- the low end of those projects came in at less than $10,000 of flowing barrel. Then there were some progressively higher ones. I think, on average, they average just below $25,000 of flowing barrel. That's the sort of ballpark we're talking about. These tend to be significantly lower than grassroots costs. You just find that bit of the plant which needs bottlenecking. We know, because we specifically designed it at Fort Hills, that we designed the front-end mining and primary extraction, we designed it bigger than the back-end because we wanted to bring the plant up quickly and then we want it to have a high reliability factor on it. So we spent some funds in doing that. So we know we've got some opportunity there to debottleneck right now. So I would think of those and the Syncrude ones is in that $25,000 of flowing barrel as a good marker for now. And as we get nearer to the specific projects, we'll update on that.

Roger D. Read *- Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

Great. And then a question on the reliability side. Obviously, you had the plant turnaround here accelerated and then the unplanned outage. What should we be looking for on the outside, in terms of ways we'll know that, that reliability is being improved as opposed to 2 or 3 years from now, we can do a look-back and say, well, yes you got better? What are some of the markers we should be watching for?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

We will talk to it. I think we owe you a more detailed presentation on what the individual components are. Those 70 -- some of those 70 line items that are specifically around reliability and improving service factors, you will see it. So I think, what you'll see is if you look at the third and fourth quarter, they were the best 6 months of the operation in Syncrude's 40-year history. You will see quarters where that will start to happen. And of course, the secret then is how do you do that continuously. We know the plant is capable of it. We know that the hydraulic capacity is there. It's a question of how you do day after day, week after week, month after month. So you will start to see it come through, and you'll start to see us guide on improved throughputs or reliability and you'll start to see costs coming down. It won't be just big steps, you'll actually see a trend start to occur.

Operator

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And our next question comes from Paul Cheng from Barclays.

Paul Cheng - ***Barclays PLC, Research Division - MD and Senior Analyst***

Steve, when you earlier talked about the replicator for the new SAGD project extension by maybe early 2020, what may be the factor, if there's any, that could push the time line earlier or later?

Steven W. Williams - ***Suncor Energy Inc. - CEO, President and Non Independent Director***

Several things, Paul. I mean, first of all, we won't rush it from a technical point of view. So what I mean -- 2 important components of the projects at the moment are, we have -- the technology developments are coming along very nicely, and we're putting tests in -- large-scale tests on the technology itself; very encouraging, done very well. So we're looking at how we will install that technology as we bring the project on. And that's the combination of the solvent-type technology and the electromagnetic wave technology. So we're just looking at the final designs of those applications. That's one piece. The other piece is we're working with contractors about how do we design this once and build it many times so that we get that -- the benefit of that replication and the benefit of almost like a manufacturing plant. We'll bring one of these 30,000, 40,000-barrel a day units on every 12 or 18 months. So we're grinding through what that execution strategy will look like in detail and having the discussions with some of those contractors. So both of those are progressing nicely. You could easily be talking plus or minus 12, 18 months on those opportunities, but very encouraging. But we don't -- we won't rush it for the sake of it.

Paul Cheng - ***Barclays PLC, Research Division - MD and Senior Analyst***

And maybe this is for both Steve and Alister. I assume that if oil price is going to move much higher than the current future strip and given that you are not spending any more money in organic CapEx than where you're currently budgeting and you don't see a lot interesting opportunity on the M&A, should we assume that you won't put the money, additional money, in the balance sheet and instead that would go for additional buyback? Or that you increase the piece of the buyback as a result?

Steven W. Williams - ***Suncor Energy Inc. - CEO, President and Non Independent Director***

I mean, all I would say, Paul, is again judge us by our track record. You'll see a mix -- I mean, Alister's eager to come in, so I'll let him speak. But you're going to see us putting the -- you've seen $1.75 billion of debt be addressed, you've seen us go into buybacks, so it's exactly the sort of mix you'll see going forward.

Alister Cowan - ***Suncor Energy Inc. - CFO and EVP***

Yes, just to reemphasize what Steve said there, Paul, I mean, it was clearly stated, our intent to increase returns to holders. So I would say that as oil prices move up, we'll be looking at the dividend again and so buybacks. And we said we wanted to gradually strengthen the balance sheet over time. So a bit of a mix, as Steve just said, yes.

Paul Cheng - ***Barclays PLC, Research Division - MD and Senior Analyst***

And final one for me. Steve, you mentioned about the 70 projects or initiatives that you guys are looking at the integration between you guys and Syncrude. Any kind of financial metric or operating metric, what is the medium term, let's say, 2 to 3 years down, what you expect this initiative will achieve in terms of whether that is reliability improvement or improving the highest realization or that reducing -- is there anything that you may be able to share at this point?

Steven W. Williams - ***Suncor Energy Inc. - CEO, President and Non Independent Director***

I mean, we tried to give actual guidance on it. So we talked about 90% reliability in 2020, and we gave cash cost guidance of about $30 in the same time frame. I mean, the first -- and we owe you more detail. I think now is probably not the time to do that, but Steve will be -- and Alister will be working on how we get some more of that detail out to you guys. The first of the projects are executed already. So we now have technical experts in working alongside Syncrude engineers. The Chairman of Syncrude is Mark Little, our Upstream President, and he is actively working on personnel exchange and the shorter-cycle projects that we can get to. So it's a bit of a continuum. First ones are actually happening right now, I mean, the first movements of material physically. I think we're moving 12,000 to 14,000 barrels a day of gas

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oil to keep the upgrader there running. And we've just recently started moving naphtha. So literally, the first project -- you won't see us come out with a comprehensive list of 70 projects and 70 time lines and expectations. What we'll give you is general guidance on what to expect in terms of reliability and cash costs and we'll give you some of the color on the detail of the projects so that you can see what we're doing and see the progress we're making. It'd be probably worth saying, Paul, just that the -- there couldn't be a better alignment between ourselves, Imperial, Exxon and the minority shareholders now; we're absolutely aligned on accelerating the program and getting to these benefits as quickly as we can.

Operator

And our next question comes from Phil Gresh from JPMorgan.

Philip Gresh *- JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

A couple of follow-ups, I guess here for me. One is just on the asset sale proceeds and the process here. You got a lot of cash in the door in the first quarter; it was a little lower than what I had in my model. I think I didn't have quite the amount of tax implication. But is it fair to say that you're kind of done with your asset sale process? Or do you still see more pruning to do?

Alister Cowan *- Suncor Energy Inc. - CFO and EVP*

Sorry, Steve, I was... Phil, I was just going to say the sale of the 49% interest in the East Tank Farm has now been completed. So that's probably the difference that you've got in your model. We don't expect to see that happening until probably Q3, but it is on track for that. So that's where we're going to be, close to $500 million.

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

So yes, and then -- so no major other asset sales planned, although the discipline you see in this exercise around looking at what is the core of our business and investing in that and then divesting of things which are not core to our business, that process is ongoing.

Philip Gresh *- JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Sure. Okay. Second question is just a follow-up on the balance sheet with the paydown here in the second quarter. As you think about your target levels and leverage and then compare it with the buyback, would you say that -- maybe to frame it as the absolute level of debt you have here, your comfort level there is high, even if oil prices were to, for some reason, go down and if OPEC were to pull back in the agreement, et cetera, that you're generally comfortable at that level? Or do you still see some room to bringing that down?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

I mean, I'll make the first comment and Alister, I'm sure, is going to want to jump in. I mean, we're setting the company up with a focus on cost reduction, general shape of the balance sheet to be able to operate healthily at $40 a barrel.

Alister Cowan *- Suncor Energy Inc. - CFO and EVP*

Yes, I mean, if you look at the level of debt, we're -- with the buyback, we'll be down to the midpoint of our range on debt to capital, and we're trending strongly down in the net debt to cash flow. So I mean, I think -- well, I see the metrics are going to continue to go down as we go forward in the next couple of years for the cash flow we're generating, even with continuing on the share buyback. So on the absolutely level, I mean, we have some opportunities in the next couple of years if we wanted to buy some of that down with some

(technical difficulty)

but I'm not particularly focused on it at this point.

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Philip Gresh *- JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Sure. Okay. And last question. For Steve, you mentioned kind of looking back, being comfortable with the decisions you made and not changing anything. And obviously, I thought the Syncrude acquisition, solid decision. I'm wondering if you look back on the equity issuance at that time, which I think was more proactive in nature to look at future potential deals, is that something that if you look back, would you still have done that piece of it? Or how do you think about that today, with now the buyback (inaudible)?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

I think that's a really fair question. I mean, I think with the -- of course, what we didn't know at the -- what we were committing to was capital discipline and a healthy balance sheet. And we did that deal. The one thing that made me feel very comfortable about that deal was that most of it was bought by our existing shareholders when the allocation was done. So some of the issues that could have been there were not at the fore. So but when I look back now with the benefit of hindsight, we were probably being very conservative at that time. And we've always committed to keeping the balance sheet healthy because we think it's a strategic asset, but I think that's a fair question, Phil.

Operator

And our next question comes from Fernando Valle from Citi.

Fernando Valle *- Citigroup Inc, Research Division - VP and Senior Analyst*

First, I wanted to dig in a little bit on the earlier question on the refining outlook. You have very strong demand growth on your marketing sales. I just wanted to understand if that was more on market share gains or if you saw a better demand outlook in Canada than we've seen in the U.S. this year?

Steve Douglas *- Suncor Energy Inc. - VP of IR*

Fernando, it's Steve Douglas here. I think, probably on the distillate side, we saw a strong comeback. And certainly in Western Canada, a big part of distillate demand is the industry itself. It's drilling rigs coming back on and the associated trucking and railcars. So we saw a strong return on that demand. Also saw it in the U.S., where distillate demand had been in decline last year, and we saw that come back strongly. We did see a bit of weak gasoline at the beginning of the year, but subsequently, that came back. So yes, I would say in Canada, a little stronger than the U.S. across the complex.

Fernando Valle *- Citigroup Inc, Research Division - VP and Senior Analyst*

Great. And then bigger picture, long term, Steve, you talked a little bit about a delay in the -- thanks to the new projects through 2020. I just wanted to understand when you do see new SAGD projects coming online, what are you trying to accomplish, just a lower overall breakeven or are you trying to change the payback structure by shortening paybacks? Do you think the technological breakthrough or is it just be able to differentiate Oil Sands paybacks or just overall breakevens?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

I think, first of all, I would say -- I mean, what I'm talking about are the final full ASC approvals. We are actually spending funds on those projects now both in terms of the technology development, the early design of some of those projects and doing real work with contractors about how we get the benefits. So those things, we're not spending anything. Part of that $5 billion we've talked about includes investment to develop the technologies, pilot the technologies and then move seamlessly into the operations of the plants. But really, I mean, it's focusing on a number of things. I mean, it's generally to improve the economics, so it's getting the best technology, which will manifest itself in a number of ways. Reduced capital costs, so we're -- by designing once and building multiple times, you reduce those costs. Better operating costs, because you are seeing the -- some of these are moving towards little if no steam, depending on our final design. So you're seeing the operating costs of these units come down. So overall, you're going to see the actual capital cost involved coming down, that's one benefit; and you'll see the returns on these projects coming on.

Operator

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And the next question comes from Nia Williams from Thomson.

Nia Williams

I wanted to ask about what your thoughts are on President Trump's comments about energy potentially being the target of trade sanctions? And what steps, if any, Suncor would take if that situation were to continue?

Steven W. Williams *- Suncor Energy Inc. - CEO, President and Non Independent Director*

I mean, first of all, I won't comment on the hypothetical situations. But clearly, there are discussions going on across the board on all sorts of trade. Of course, the oil trade is a very balanced trade, and there are serious potential consequences to customers and the general population [voters] in the U.S. if tariffs or border taxes were to be implemented. I think the general view is that the probability of it on energy is relatively low; not to say impossible. The one thing I would say for Suncor, not surprisingly, we've done a fair amount of analysis on what it could look like. And with -- the impacts for Suncor, not the industry necessarily, are fairly mitigated because, of course, we have an integrated business, we both import and export materials across the border. We have operating businesses in the U.S. itself, which would be inside. So the impact for Suncor itself relative to the industry will be fairly muted.

Steve Douglas *- Suncor Energy Inc. - VP of IR*

And with that, we've reached our time. So thank you very much for participating. Appreciate the questions and of course, as always, we're available for further detailed questions throughout the day and going forward. Thank you, operator.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. And this does conclude the program. You may all disconnect. Everyone, have a great day.

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