MINISTERIAL INTERVIEW

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Moderator: Manus Cranny, Anchor, Bloomberg TV

Mannus Cranny (MC): *Your Excellency, is the Saudi Aramco deal to buy PIF's stake in SABIC one of the seminal moments of transformation for Saudi Arabia?*

Khalid Al Falih: The kingdom is going through a phenomenal transformation. You see it in social activities, in economic activities, amongst the youth, amongst business enterprises. You see it present in the reforms and every government agency. And you see it in the sound strategies that have always been on paper but that have previously found difficulty in getting implemented. Vision 2030 is now making it possible to implement these and one of those has been the dream to create the world's largest oil and energy petrochemical companies. As a former CEO of Saudi Aramco, we had a vision within the company to create an integrated energy petrochemical giant that would add value to the hydrocarbon value chain. SABIC is the way to do this because there is a lot of overlap geographically and in terms of the molecule flow from upstream to midstream to downstream, as well as complementarity between the two portfolios. It would have been unthinkable a few years ago because SABIC has always been seen as a national champion with a standard of their own. But with the vision of breaking barriers and paradigms, it is now turning into a reality. This acquisition will realize synergies and integration opportunities not just for Saudi Aramco, but more importantly for SABIC and its minority shareholders. So, it is value creation all round and we hope to close the SABIC deal in the coming six months.

MC: *Will the funds that flow from this deal reenergize the ambitions of the kingdom to deliver on Vision 2030?*

Khalid Al Falih: The vision of the PIF is very bold and goes way beyond the $69 billion that Saudi Aramco will provide through the SABIC deal. The vision is both domestic and global. It's about the mega projects that will turbo charge many of the pillars of our future economy. This will need capital also from other assets that are non-strategic, that the PIF may own that they choose to exit.

MC: *What kind of assets?*

Khalid Al Falih: It's premature to specify, but my point is that the PIF is going to be an active and not a passive investor. The objective is to create value for the kingdom, first and foremost, through in-country investments and also by looking globally and strategically to acquire emerging companies and industries, creating value for them. At the same time, leveraging those acquisitions and investments for the benefit of the kingdom's strategy.

MC: *Was the recent Saudi Aramco bond roadshow a curtain raiser to perhaps coming back to the bond market again?*

Khalid Al Falih: I think Saudi Aramco will establish a permanent presence in the capital markets that will have both debt and capital. It is the world's largest company and is obviously going to have all the tools at its disposal to access capital markets. Paying for the SABIC deal was not the primary or only reason for accessing the bond market; the company needs to lever up and have some debt and instruments on our balance sheet.

#1
Saudi Aramco is the world's largest company.

$69bn
The volume of finance that Saudi Aramco will supply as part of its purchase of PIF's stake in SABIC.

x2
There are two dimensions to the kingdom's gas plans. Firstly, to increase domestic production, including shale gas reserves, and to leverage gas as the preferred feedstock for the rapidly growing petrochemicals market. Secondly, to sharpen the kingdom's competitive edge in the global gas markets.

2025
The kingdom, already the world's biggest oil producer, plans to be a significant gas exporter by 2025.

9.8bn
The global population will climb by more than 2 billion - a 27% increase - by 2050 to 9.8 billion. This is the equivalent of nearly duplicating the entire population of China and India, the world's most populated nations, by mid century. What does this mean? Investing in lower-carbon energy - gas, LNG and renewables, for example - to meet rising demand is a safe bet.

MC: In terms of the kingdom's economic transformation, what are the ambitions for gas?

Khalid Al Falih: There are two dimensions to gas. One is domestic where gas is the feedstock of choice for our petrochemicals. It's low cost to crack and it's plentiful and it's reliable and we need to increase that. There is also a second wave of gas development that has emerged over the last few years by Aramco, which is to develop our own unconventional resources, mostly shale gas, in eastern Saudi Arabia, but also other formations in the north that have been used to fuel phosphate mining and manufacturing development. Gas is also the fuel of choice for power generation, so dry gas or natural gas will be used to displace 600,000 – 800,000 barrels of liquids that are going mostly to power, but some to water desalination. Both sectors will be reformed, and their efficiency improved dramatically, by changes in the fleet and power generation by switching a lot of our water desalination to reverse osmosis technologies. The second dimension for gas is global. We realize that oil will continue to grow, but gas will grow faster.

MC: Does that mean that you'll have to buy assets globally?

Khalid Al Falih: Anything in excess of our domestic needs in power, water and petrochemicals, will be exported. We do see an opportunity to be a significant gas exporter.

MC: How soon can you achieve that?

Khalid Al Falih: I would say by 2025 is realistic. We're already in discussions with our brothers in the GCC about interconnection through pipelines, all the way from Oman to Kuwait and Iraq.

MC: Have you committed a capex number to that?

Khalid Al Falih: Not yet, but we've dedicated the teams from our side and our colleagues from the GCC have indicated that they're ready to start undertaking the technical studies. I think what will happen after that is the commercial framework through which gas is traded through pipelines in the region and this will be a significant move forward that the kingdom will enable because we are the country that interconnects most of the GCC countries and Iraq as well. The next phase beyond this is LNG trade. We know that growing and sizable economies around the world, from China to India and other countries in Asia, will need to displace a lot of their existing coal generation facilities to meet their climate change targets. But we also know that there are billions of people who don't have access to clean energy and with population growth set to increase by another 2 billion, the demand for this is set to increase. Clean energy is going to be a combination of gas and renewables and the kingdom is ready to play a leading role in these emerging economies.

MC: What has changed that Saudi Arabia now wants to make the commitment to be a gas exporter in a few years? Has there been a significant shift in terms of policy?

Khalid Al Falih: The resource base has changed for us. We have always looked at conventionals as the limit of resource availability and we've always thought of ourselves as resource constrained. With the unconventional gas resources going deep into the shale formations in the kingdom, we are not only able to access natural gas, but wet rich gas that is going to power our growth for the petrochemical industries as well as give us these resources. We are also able to produce some associated gas at higher levels now. ■

**Edited transcript*

IN FOCUS: OPEC+

MC: Will the group extend output cuts beyond June this year?

Khalid Al Falih: Our objective to bring inventories back to a reasonable level remains unchanged. We have seen how sensitive oil markets are to inventories and how when production is increased in the second half of the year for the usual reasons, how quickly markets react. We want to avoid that scenario materializing again. Given the kingdom's financial position and our scale, our volumes can probably withstand some of these shocks more than others. We have seen companies having to change investment plans and some of the poorer countries hurt, so we want to stabilize markets. We are getting to a stage where inventories are starting to stabilize and come down, but they're still significantly above what I would consider a normal level.

MC: Is 1.2m barrels still your baseline to balance the market?

Khalid Al Falih: The 1.2m barrels was based on certain other countries keeping their October 2018 production level. So, we have to watch them. We need to see what happens with Venezuela and with the sanctions, which the US waived in November. All these factors will impact the fundamentals. Ultimately, the 1.2m barrels was a balancing based on assumptions of demand and supply and US production. The closer we are to June, the more informed our decision will be on the next steps.

MC: Is Russia on board in general about a possible extension?

Khalid Al Falih: The dynamics in Russia are different from any other country. It also has different geopolitical considerations than most other producers, so it has to weigh all of those factors. But I believe strongly that the OPEC + agreement has been good for Russia from multiple angles. As a key producer, it holds a lot of resources, not just oil but gas as well. The value of gas in the international markets is impacted by the oil outlook and oil prices.

MC: You've been producing 9.82m barrels, which is a four-year low. Many people are applauding you and saying you have done the big job. Are you prepared to cut further to achieve market balance?

Khalid Al Falih: If you look at 2017-2018, by the time it was all said and done, the kingdom was almost exactly on the dot with the voluntary production level that we agreed to back in December 2016. During that two-year period, we were able to stabilize the market's response with market dynamics that changed unexpectedly. But at the end of the day, we were on track and we met our obligations. The kingdom is the world's largest exporter and the country that has, by far, the largest spare capacity. With our policy and the relationship that we have with the industry within the kingdom, we're able to swing production faster than ever, so we're driven by our policy objectives of stabilizing markets. Sometimes we do more than others, but it goes both ways.

MC: Would you be prepared to do more if you needed to?

Khalid Al Falih: The market is on its way towards balance. We've obviously done a lot more than others, but I've been assured that they're catching up with their obligations. I was in Iraq a few days ago and the Minister reassured us that Iraq will do more and would be on track. Russia has reached its objectives on its commitment and the UAE and Kuwait have too. The majority of countries have met their obligations and the implementation is moving in the right direction.

MC: Are you comfortable with the recent speed of recovery in the oil price?

Khalid Al Falih: Our policy has never been, nor will it be, driven by price objectives and we always need to look at what the appropriate baseline is to measure from. We can feel it when the market is healthy. We can feel it when investors are comfortable. You saw in early April that for the first time in almost two months, the number of rigs in the US rose. Many would consider this bearish, but I would consider it as one of the vital signs that the market is coming back to health.

MC: What is the most under-priced risk for the market in your mind? What's the next shoe to drop?

Khalid Al Falih: Geopolitical risk. There are times when the market overprices this and times when it under prices it. It's unfortunate that many countries – from Venezuela to Algeria and Libya, Syria and Yemen, all of which have oil – are in civil and security distress. That could squeeze supply in the mid to long term if things don't improve. But given the fact that we have a glut today, the market seems blind to that risk. The saving grace is that the spare capacity that the kingdom has means we can always reduce the level of cuts like we did last year.

Up, Up and Up

We see strong demand in the emerging economies of Asia. The US' economic GDP growth can drop by a percent or two, but the underlying drivers for oil demand will continue. The demographics are there, the urbanization is there, people are moving from rural to big cities and acquiring modern modes of transport and lifestyles. That's not going to be dented significantly by GDP growth on a sustainable basis. I think where demand could flatten and weaken a bit is in the Organization for Economic Co-operation and Development (OECD) countries, where manufacturing and trucking and industrial activity are the main drivers. And there are a lot of incentives that are being put by governments to reduce demand (through taxation). But there's a limit to that too and it is not a line that is going to remain linear indefinitely. Even in the US, which is a highly industrialized economy, demand will continue to grow. *Khalid Al Falih*

"We realize that oil will continue to grow, but gas will grow faster"

800,000bls
Leveraging the kingdom's natural gas reserves can save 600,000 – 800,000 barrels of liquids that are currently being used for power generation, as well as some water desalination projects.