How does an international business change when its core commodity drops in price?

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Good morning Ladies and Gentlemen.

Thank you Lord Leaman for the introduction and for the invitation to join you today.

It is a pleasure to be here in what I understand is an auspicious year for the MCA.

I know you act as the respected voice of the industry, as an assurance of quality, and as a forum for sharing best practice.

And the fact you are celebrating your 60th anniversary suggests you are doing all of that very well. So congratulations.

In preparation for this morning I was thinking about challenges we have in common, and one stood out – particularly at this time.

It is the challenge of the information age.

Since I stood up 30 seconds ago, over 70 million emails have been sent worldwide. Over 2 million posts have been liked on Facebook. Over 25,000 apps have been downloaded by Apple users.

We each have our own tidal waves of information from which to extract the data, insights and trends that will enable us to plan ahead.

Understanding the context is especially important as we seek to navigate very challenging conditions and chart the right course for the future.

But of course, none of us can literally predict the future.

And the truth is that none of us knows exactly what the oil price is going to be in six weeks' time, let alone six months or six year.

The best we can do in terms of forecasting is to understand the trends and form a view on the most likely course of events. However, there are always uncertainties that may shift outcomes away from the most likely course.

The business world is always prey to what Harold MacMillan called ‘events, dear boy’ – or Black Swans as they have been described more recently.

So forecasting can only take us so far.

The sustainable solution lies not in prediction, but in preparation.

The answer is to build a business that is good for all seasons. One with the capacity to cope with anything the world can throw at it.

In BP we have a distinctive model for managing uncertainty and change which has served us well over many years. It has four pillars:

First, **resilience** – in our operations and financial framework;

Second, **focus** – in our portfolio;

Third, **capability** – in our people;

And fourth, **partnership** – through our relationships.

Lower for longer

I’ll discuss those factors in a moment, but let’s first take a look at the current context and what has changed.

In March 2014 the oil price stood at $112. A year ago it was $55. And this week it has been around $35.

In other words, revenues from oil have fallen by three-quarters in under two years

To know how best to respond, we need to understand the cause of the change – and to distinguish between what is new, and what we have seen before.
The really major new development of recent years has been the shale revolution in the United States, which has caused the oversupply in the global market.

For an unprecedented three years in a row, US production increased by an average of one million barrels a day – with the effect that in 2014, the US overtook Saudi Arabia to become the world's largest oil producer. This has created a new dynamic in the industry.

However, in other ways, we are in familiar territory. When I joined the industry in 1989 the price of oil was around $18 and since then I have seen four major price shocks.

So anyone who has experience in the sector has learned that volatility, while it can be dramatic, is in fact normal.

New developments like shale become absorbed and the fundamentals reassert themselves.

Already we are seeing US production coming down and prices edging up, and we believe that supply will converge with levels of demand sometime in the second half of this year.

As we have consistently said, prices are likely to remain lower for longer – but not forever.

Demand too, has followed a reasonably predictable path. We expect it to grow a little slower in the next 20 years than the last 20 as emerging countries rebalance their economies, but nonetheless, we still anticipate demand being around a third greater than today by 2035. That is like adding two more USA's to current consumption.

And this is due to continuing economic growth in the emerging economies, driven by increased productivity as well as rising populations.

So the general picture is that we remain on a demand curve that is still steadily rising as part of an inexorable long term pattern, although shorter term oscillations in supply and demand can create volatile conditions.

Resilience

So let me now return to those four pillars of adaptation I mentioned.

The first is to create a business that is truly resilient, operationally and financially. This means a combination of increasing efficiency to minimise today's costs while continuing to invest in a disciplined way for tomorrow's growth.

In BP, we have spent the past few years building capacity in safety, reliability and greater efficiency – and over the last 18 months we have simply accelerated this drive in response to the changing environment.

We have taken steps to simplify the business, challenging everything from IT systems to warehousing to see if we can manage with less complexity and less cost.

But we have also continued to invest in a very disciplined way, sanctioning only the highest quality projects and then spending each dollar of capex as effectively as possible.

So, despite the lower oil price, we have recently signed agreements for major new investments in places such as Egypt and Oman that will generate value for decades to come.

Focus

Let me turn to the second pillar of our adaptation strategy which is focus in respect of the portfolio.

Since 2010 – by way of illustrating this focus in practice – BP has sold around half of our upstream installations and pipelines and one third of our wells, as part of a $75 billion divestment programme. But in doing that we have retained around 90% of our proved reserves and production and in fact we increased operating cash flow by 50% between 2011 and 2014.

This shows how the right assets, focused on the right strengths, can maximise value in tough market conditions – particularly when coupled with the right performance.

We call it putting value over volume, targeting value creation rather than simply production.

A few years ago people were suggesting we might improve focus by demerging our Upstream and Downstream businesses. But last year, our Downstream earned $7.5 billion compared with $1.2 billion in the Upstream. That showed the benefits of being a focused yet integrated business, where falling prices may challenge one side of the business but benefit another.

Capability

The third pillar of our approach is capability and – as with resilience and focus – this is closely linked to the portfolio.

In BP, we rely on our operational capabilities in areas such as deep water, gas supply, giant field management and tight gas. We built these skills over decades but particularly after the nationalizations of the 1970s when we were obliged to go to new frontiers such as the North Sea and Alaska and develop new skills.

And these operational strengths are complemented by functional capability in strategy, finance and trading.

These are the reasons why governments and national oil companies ask to come and work with them.

And it is very important to invest in specialist capabilities when times are good because these enable a business to operate at maximum efficiency when storms come along.

You probably heard the story of the CFO who asks the CEO, "What if we invest in developing our people and they leave?" In reply the CEO says, "What if we don't invest in them and they stay?"

Capability is particularly important in management because a company's strategy, direction, character and financial framework are formed by the collective experience and expertise of its leaders.

You can outsource activity – from the drilling of wells to customer service – but you cannot outsource decision-making.

Partnership

This takes me to the fourth factor in the process of adaptation – which is partnership.

Competitiveness doesn't just come from your own strengths, but also from the strength of your relationships – with partners, with governments and suppliers.

The new agreements I mentioned earlier in Egypt and Oman – those have been made possible by the long-standing relationships we have with governments in those countries.

We are also working with our supply chain in a number of ways to bring costs down.

I many cases we negotiate lower rates in exchange for longer terms – a so called ‘blend and extend’ approach.

We are also looking to simplify and standardise procedures and to renegotiate contracts – and that comes about through mutual respect on both sides.

Just to give you one example, a few years ago, we costed our Mad Dog Phase 2 project in the Gulf of Mexico at $20 billion.

We have worked with our partners on new project phasing, simpler design and common industry solutions instead of bespoke ones.

We’re now costing the project at less than $10 billion.

We are also looking to build much deeper operational partnerships that deliver step changes in safety and reliability.

In one recent example, we brought together a crew consisting of staff from BP and contractor companies to practise safety and drilling procedures in a state of the art simulator that replicated the condition of offshore operations.

The result was that the team went on to safely drill the most efficient wells for a decade in the Nile Delta.

Conclusion

To summarise, I suggest there are four key factors in navigating turbulent times such as these.

Operational and financial resilience – based on safe, reliable, efficient operations.

A strong portfolio with a focus on value over volume - one that can generate value at the bottom of the cycle as well as at the top.

Deep levels of capability, allied to technology - providing flexibility and adaptability.

And strong partnerships – so the burdens can be fairly shared and partners can work together to deliver excellent performance needed to prevail in a tough climate.

This is not the first time we have to manage a turbulent present and an uncertain future and it will not be the last.

Uncertainty is a constant in our business. You cannot evade it and you can either fear it or you can embrace it. I prefer to embrace it.

Thank you and now over to you for your questions.