FitchRatings

RATING ACTION COMMENTARY

Fitch Upgrades Occidental Petroleum Corp.'s Long-Term IDR to 'BBB-'; Outlook Stable

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Fitch Ratings - Chicago - 16 May 2023: Fitch Ratings has upgraded Occidental Petroleum Corp.'s (OXY) Long-Term Issuer Default Rating (IDR) to 'BBB-' from 'BB+', and upgraded OXY's senior unsecured ratings to 'BBB-' from 'BB+'/'RR4.' The Rating Outlook is Stable. The main driver of the upgrade was the improvement in midcycle credit metrics, stemming from the combination of incremental de-leveraging, along with anticipated improvements in midcycle earnings in the chemicals and midstream segments.

OXY's ratings reflect its large size and liquids-weighted profile, competitive netbacks, anchor position in the Permian, and the impact of ongoing deleveraging activity. The ratings also reflect a manageable maturity wall, and above-average diversification versus upstream peers, including chemicals and midstream. Rating concerns include somewhat elevated interest costs and debt relative to peers, higher near-term capex spending, uncertainty around funding and costs for OXY's low carbon ventures, and the potential impacts of a macroeconomic slowdown.

KEY RATING DRIVERS

Redemptions Improve Coverage: The main driver of the upgrade was incremental deleveraging. In Q1, OXY announced it accrued redemptions for $647 million in preferred stock, eliminating an incremental $52 million in run-rate dividend expense. The rules around preferred redemptions are onerous, and include the need to maintain a $4.00/share pay out on a rolling 12-month basis, pay a redemption price of 110%, and repurchase an equal amount of preferred stock for common share distributions. Fitch anticipates the company will maximize the current window and purchase additional preferreds in 2023, but may switch back to debt repayment in 2024, assuming lower oil prices. In addition, the company repaid an incremental $22 million in 8.75% notes in Q1. Cumulatively, since the close of the Anadarko acquisition, OXY has retired over $26 billion in debt, including $10.5 billion in 2022.

Non E&P Improvements: Earnings are set to improve in the company's chemicals and midstream & marketing segments, driven by new projects and contract roll-offs. In OxyChem, this includes the membrane conversion project at OxyChem's Battleground chlor-alkali plant, which will expand capacity by 80% by 2026. This project, in conjunction with other smaller near-term expansions, will contribute $300 million-$400 million in incremental EBITDA. OXY recently increased midpoint guidance for OxyChem's 2023 pre-tax income to $1.5 billion. In midstream & marketing, the roll-off of out-of-the money pipeline contracts is also expected to create earnings uplift beginning in 2025.

Strong 2022 Results: The combination of strong hydrocarbon prices and lower debt and interest costs has resulted in robust near-term credit metrics. As calculated by Fitch, at YE 2022, the company's EBITDA leverage declined to 1.1x, FFO interest coverage rose to 8.7x, and FCF was a record high of just over $11 billion. Contributions from midstream & marketing were limited due to continued narrowness in Midland to Houston crude differentials, but chemicals contributions were robust. Fitch anticipates positive but declining FCF generation over the next few years under our base case price deck. In line with the company's capital allocation framework, Fitch anticipates modest incremental de-leveraging as FCF will be increasingly dedicated to shareholder distributions. OXY does not systematically hedge its upstream production.

Maturity Wall Manageable: Following refinancing and debt repayments, OXY's near-term wall is moderate. As calculated by Fitch, maturities due over the next few years (excluding puttable 2036 bonds) include nothing due in 2023, $1.06 billion due 2024, $1.21 billion in 2025, and $1.45 billion in 2026. The combination of cash balances, full availability on the company's unsecured revolver, and strong projected FCF should comfortably address the near-term maturity schedule.

Integrated Producer: OXY enjoys modest but meaningful diversification through its chemicals segment, which has a top-three position in basic chemicals in North America, and its midstream segment. Chemicals have historically contributed strong FCF given limited reinvestment tailwinds due to solid domestic demand and feedstock cost advantages, as well as Russia sanctions. The midstream segment has historically been weighed down by weak Permian-Houston differentials, but the impact of these should be reduced by contract roll-offs and gradual widening of spreads in line with increasing Permian production.

Higher Capex: OXY is guiding to higher capex spending in 2023, with projected spending of $5.4 billion-$6.2 billion, an approximately 30% increase above 2022 levels, and well above maintenance capital of $3.5 billion, which itself rose from $3.2 billion due to higher production, and growth projects including the OxyChem chlor-alkali expansion, as well increased spending for Low Carbon projects. The company is seeing inflation in the upstream in the U.S. in the 15% range, with inflation in international upstream lower.

Carbon Reduction Initiatives: OXY's commitment to scope 3 emissions stands out versus U.S. E&P peers, and is centered around creating carbon sequestration hubs using its geologic formations. This includes the construction of the world's largest direct air capture (DAC) plant at 1 million metric tons of CO_2, with operation expected mid-2025, slightly delayed vs earlier estimates. While the economics of the DAC plant have improved following passage of the IRA, there is considerable uncertainty around ultimate costs and returns, as well as long-term financing plans. OXY is self-funding the first DAC plant but Fitch expects this will shift to substantial third party funding if it scales the business up. For now, OLVC does not comprise a large portion of OXY's total budget, which limits its impact on credit quality.

DERIVATION SUMMARY

OXY's debt and interest expense are somewhat higher than IG peers given the high amount of transaction debt incurred to fund the Anadarko acquisition. However, OXY has since repaid a substantial amount of gross debt, and has begun to address the preferreds. While interest coverage is likely to remain relatively low, this is offset by the company's strong business profile.

In terms of size and scale, at 1,159kboepd in production from continuing operations in FY 2022, OXY is among the largest independents, significantly larger than Ovintiv Corporation (510.1kboepd), Devon Energy (610.7kboepd), APA Corporation (386.8boepd), and Marathon Corporation (342.5kboepd). Only ConocoPhillips (1,518.2kboepd) is larger. OXY's liquids weighting at around 76% is also above average, while OXY's cash netbacks ($43.4/boe at YE 2022) are in line with diversified peers.

Geographic diversification is above-average, with E&P operations split between the U.S. (Permian, DJ/Rockies, Gulf of Mexico offshore, Powder River Basin) and international in MENA (Algeria, Oman, the UAE, and Qatar). OXY is a leading producer in the DJ Basin, the number four producer in the Gulf of Mexico, and a large Permian producer, with one of the biggest net acreage positions (2.8 million acres, split roughly between Permian unconventional shale, and EOR). OXY has additional earnings diversification through its chemical and midstream segments, which sets it apart from peers. No Country Ceiling, operating environment or parent-subsidiary-linkages constrain the rating.

KEY ASSUMPTIONS

--Base Case West Texas Intermediate (WTI) oil prices of $80/barrel in 2023, $70 in 2024, $60 in 2025, and $50 in 2026;

--Henry Hub natural gas prices of $3.50/mcf in 2023 and 2024, $3.00/mcf in 2025, and $2.75/mcf in 2026;

--Capex of $5.8 billion in 2023, which declines to just under $5.6 billion by the end of the forecast;

--Production volumes of 1.19 million boepd in 2023 rising to 1.25 million boepd by the end of the forecast;

--Company assumed to redeem $1.1 billion in 8% Berkshire preferreds in 2023 and switches back to moderate gross debt reduction over the remainder of the forecast as oil prices moderate;

--Increased FCF allocation to share repurchases and dividends, in line with company's shareholder return framework.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Mid-cycle FFO interest coverage approaching 7.5x;

--Mid-cycle EBITDA leverage below 2.2x;

--Material incremental reduction in interest expense or gross debt levels.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Mid-cycle FFO interest coverage approaching 5.0x;

--Mid-cycle EBITDA leverage above 3.2x;

--Shift towards a less conservative financial policy.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Cash on hand as of YE 2022 was $984 million, excluding restricted cash of $42 million, and there was no draw on the company's committed $4.0 billion senior unsecured revolver due June 30, 2025, for core liquidity of just under $5.0 billion. The only financial covenant associated with the revolver was a max debt/capitalization ratio of 65%.

Separately, OXY had full availability on a $600 million accounts receivables securitization facility, which is subject to monthly redetermination and matures December 2024. OXY's maturity wall is manageable given the impact of recent debt repayments focusing on 2022-2026 maturities, as well as good liquidity and strong projected FCF.

ISSUER PROFILE

OXY is a large diversified E&P with upstream operations in the U.S. (Permian, DJ, Gulf of Mexico (GoM), Powder River Basin) and MENA n (Algeria, Oman, the UAE, and Qatar). Non-E&P segments include chemicals (OxyChem) and Midstream and Marketing.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Occidental Petroleum Corp.	LT IDR	BBB- Rating Outlook Stable	Upgrade	BB+ Rating Outlook Positive
senior unsecured	LT	BBB-	Upgrade	BB+

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporate Hybrids Treatment and Notching Criteria (pub. 12 Nov 2020)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub. 09 Apr 2021) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 29 Oct 2022) (including rating assumption sensitivity)

Sector Navigators: Addendum to the Corporate Rating Criteria (pub. 13 May 2023)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

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Occidental Petroleum Corp.	EU Endorsed, UK Endorsed

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