



Fourth Quarter 2023 Financial and
Operating Results Q&A Webcast
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Internally Generated Transcript

C O R P O R A T E P A R T I C I P A N T S

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P R E S E N T A T I O N

Operator

Greetings. Welcome to SM Energy's Fourth Quarter 2023 Financial and Operating Results Q&A. At this time, all participants are in a listen-only mode. A question and answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press “*” “0” on your telephone keypad. Please note, this conference is being recorded. I will now turn the conference over to Jennifer Samuels, Vice President – Investor Relations & ESG Stewardship. Thank you. You may begin.

Jennifer Samuels

Thank you. In today's call, we may reference the earnings release, IR presentation, or prepared remarks, all of which are posted to our website. Thank you for joining us this morning to answer your questions. Today, we have our President and CEO, Herb Vogel, and CFO, Wade Pursell.

Before we get started, I need to remind you that our discussion today may include forward-looking statements and discussion of non-GAAP measures. I direct you to slide two of the accompanying slide deck, page seven of the accompanying earnings release and the Risk Factors section of our most recently filed 10-K, which describe risks associated with forward-looking statements that could cause actual results to differ.

We may also refer to non-GAAP measures. Please see the slide deck appendix and earnings release for definitions and reconciliations of non-GAAP measures to the most directly comparable GAAP measures and discussion of forward-looking non-GAAP measures. Also, look for our 2023

10-K, which was filed this morning, and with that, I will turn it over to Herb for brief opening commentary. Herb?

Herbert Vogel

Thanks Jennifer. Good morning and thank you for joining us. While we're waiting for people to join the call, let me start by reiterating a few key messages. Our excellent 2023 operating and financial results were driven by our very high-quality asset base, best-in-class operational performance that is supported by differential technological expertise and a track record of success, and our strong balance sheet and low leverage that enabled significant growth and return of capital to stockholders.

As we look through 2024, we are excited about our capital program, which we expect to deliver more on each of these strategic objectives as we lean activity towards the Midland Basin, where we will generate higher oil volumes and delineate and develop our new acreage positions to organically grow inventory and create value.

In short, the operational focus in 2024 is more oil growth, less gas growth, significant capital efficiency improvement with a 10% increase in capital against a nearly 30% increase in turn in lines weighted to oil. So let me say that again, it's a 10% increase in capital against a nearly 30% increase in turn lines weighted to oil. With that, I will turn it back to the operator to start taking your questions.

Operator

Thank you. We will now be conducting a question and answer session. If you would like to ask a question, please press “*” “1” on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press “*” “2” if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the “*” key. One moment please, while we poll for your questions.

Our first questions come from the line of Tim Rezvan, with KeyBanc Capital Markets. Please proceed with your questions.

Timothy Rezvan

Good morning folks and thank you for taking my questions. I'd like to start to on the acreage map you put out with the stealth play location. I was wondering if you could comment on what initial zones you're targeting in that Western Sweetie Peck area. And if you look at the map, there seems to be fill-in opportunities. Is that position built out? Are you still sort of looking to add? You know, trying to understand how to think about that over the next couple of years.

Herbert Vogel

Yeah, Tim, great question. We are really pleased we added those 9,100 acres there and we have this track record of our geoscience team being able to identify intervals that are kind of overlooked

a little bit by others. In that area, we have some confidence from some data we have from some offset wells. So we're not disclosing specifically which intervals we're chasing there, but we are planning to put a rig out there this year, and we'll be hopefully showing some results there later in the year. But you're right, it's easy for us from an efficiency standpoint because it's pretty contiguous with our Sweetie Peck position, so we really like what we got there. If we could add more, we would add more. It's obviously going to be pricier in the future than it was when we picked up the acreage.

Timothy Rezvan

Okay. Okay. That's fair. And then, I guess I'll pivot with a follow-up to the other emerging area that northern part in Dawson. Can you just talk about as you sort of the early stages of development, I believe, Herb, this was-the Dean was sort of the primary target here. Does that sort of remain the case? Is that what this was underwritten on? And can you talk about other areas that you may be targeting with sort of initial development?

Herbert Vogel

Tim, that's right. When we announced the acquisition in June last year, we talked about two intervals. One was the Dean and then the other was the Middle Spraberry sand. You're probably aware there's another operator just to the northwest playing the Middle Spraberry sand pretty heavily. So we'll be looking at both those intervals.

We're starting with the Dean. I think we talked about eight to nine wells on three pads. And you'll start seeing some results in probably 3Q, because we'll wait until we get past 30-day lps, but yeah, we're excited about it. And you're aware our best wells, some of the best wells in the Permian overall are in the Dean, and so we're really looking forward to the results there.

Timothy Rezvan

Okay. Thank you for the color.

Operator

Thank you. Our next questions come from the line of Leo Mariani with Roth MKM. Please proceed with your questions.

Leo Mariani

Hi. I wanted to maybe just stay a little bit with some of the new acreage here. Just curious as to kind of why you decided to disclose the 9,100 acres in terms of where that is here today and also, I was hoping you could provide a little bit more color on how you guys managed to add the 65

Austin Chalk locations. Was this just an appraisal of additional acreage from the '23 drilling program? Any color on those things would be great.

Herbert Vogel

Yeah. Hey, thanks, Leo. Yeah, pretty straightforward on the 9,100 acres. It becomes public when we file in the leases. It was already coming out there for people who were looking at the court houses, so that became public, what was not public is exactly what we're targeting drilling so we did want to disclose with everybody on a level playing field that it's really in Upton and Crane counties there.

On the Austin Chalk, it's great you picked that up. We've had such great success with delineating and then developing and now really staggering between two landing zones. That's where we've really optimized, and so we've got confidence to increase the inventory. We kind of always held that back knowing it was the potential there, and so we feel good about those additional 65 locations. It's just turned out to be a great value add that was purely organic and no additional lease acquisition cost.

Leo Mariani

Okay. That's helpful. And then, I was hoping you could maybe address first quarter production. Obviously, it's down a little bit, per your guidance. You guys did mention weather in your press release, which is certainly plagued the industry. I was hoping you could kind of maybe quantify that. Is there like a BOE per day impact on the weather side? And then, I'm also assuming that perhaps maybe there's fewer TILs this quarter, and the program is maybe a little bit weighted to subsequent quarters on TILs, so any kind of color around you got the slightly weaker first quarter production would be helpful.

Herbert Vogel

Yeah. Leo, if you guys were really tracking 2023, you know we had 92 net TILs and there were only 11 net in the fourth quarter, so that's obviously going to have an impact on the first quarter. So if you were really watching what--when we turn the wells in line in the fourth quarter, you'd see why that impact was in the first quarter. Then there was a little bit of, not a major impact, but there was a weather impact. That was partly weather itself, but then also some gas plant weather impacts on the third-party downstream for us. But that's really what drives it. And if you see what we project for 2024, you see it start from a low and then we gradually work our way up through the year. And I hope people are taking that strategic perspective of how much we produced in 2020, 2021, '22. '22 to '23 was a 5% BOE growth. And then, now we're looking at 3.5% BOE growth and 6% oil growth into '24. So I think really more focused on what are we doing overall

annually and why that is beneficial for stockholders is really more important than the quarterly cadence.

Leo Mariani

Understood. Thanks, guys.

Operator

Thank you. Our next questions come from the line of Zach Parham with JPMorgan. Please proceed with your questions.

Zachary Parham

Good morning. My first question is just on the buyback, which slowed a little bit this quarter despite some pretty robust free cash flow generation. Can you just give us any detail on why you slowed down with the buyback pace this quarter and maybe just detail how you're thinking about utilizing buyback in 2024?

Wade Pursell

Yeah, good morning, Zach. It's Wade. Good question. Nothing really tangible to report there. As we were moving into looking at 2024 and putting our plan together and a lot of uncertainty, economics and commodity prices, it just felt really good to end the year with a really strong balance sheet, which we did. Good cash position, lower leverage below \$1 billion net debt.

As we move into this year, we're still very committed, obviously, to the stock buyback program. completing the commitment of over \$200 million. And I should just say, I don't think it will surprise you that we still believe the current stock price is undervalued and the buybacks are very attractive and we will continue that as we move into 2024.

Zachary Parham

Thanks, Wade. And then my follow-up just on the M&A that we've seen in the industry over the last several months, I think there's a broad agreement that larger scale attracts a larger investor base for E&Ps. How do you see SM fitting in going forward? Do you see yourself as more likely to get larger through acquisitions or potentially combined with a larger operator? Or do you think you have the needed scale to attract more investors?

Herbert Vogel

Yeah. Zack, it's obviously a topical question given the recent consolidation in the industry. We've been there saying for a long time that we truly believe in consolidation. We see the merits of consolidation and we're agnostic as which side of a transaction we wind up on. But we do focus on kind of our area where we're really strong. So it's got to be comparable sort of inventory to ours in terms of quality that we don't want to combine where we have delayed development. We don't want to--we basically want to have a good balance sheet coming out of any sort of

transaction. It's got to have industrial logic too, if it's just two disparate companies getting together for scale, that's probably not going to move the needle for us. So that's how we look at it from a consolidation standpoint. There's clear benefits, and we'll see what comes on.

In terms of growing the company, we've been really persistent and patient about it. We have a lot of confidence in our technical team. They continue to identify organic opportunities and we wind up delivering them. And then we have that track record, had a lot of discipline in what we've done with our capital. And we sit on 10-plus years of inventory, so we don't have to really overpay to get something to just move along. So that's kind of our perspective on it. But if the right deal comes along, we'd be there.

Zachary Parham

Thanks, Herb.

Herbert Vogel

You bet.

Operator

Thank you. As a reminder, if you would like to ask a question, please press “*” “1” on your telephone keypad. Our next questions come from the line of Oliver Huang with TPH. Please proceed with your questions.

Oliver Huang

Good morning all, and thanks for taking my questions. I think just kind of to start out, in the Midland, I know last year, you all had a few Leonard and Woodford wells that you all were testing. It doesn't sound like those, or not Woodford, Wolfcamp D wells that you all were testing. It doesn't sound like those will be part of the plan for 2024, but is there any way that you all could kind of speak to how that capital might shift around from an interval targeting basis for 2024?

Herbert Vogel

Yeah. Oliver, this is Herb. Yes. The Leonard, we've had a total of six wells. Some offset operators also had some wells in there, and when we looked at the results, we recognized that it was more capital efficient to put a little--a few more wells into the Middle Spraberry, which underlies that interval. So that seems to be the right way to go about this. So the fracs will grow into the overlying interval, and that's how we would see some of the Leonard oil being produced as a more capital-efficient way. And that's just what you do in the normal course of development optimization.

In the case of the Wolfcamp D, it's a completely isolated interval. So what we've really done is delineated the Wolfcamp D, so we have a good sense of how much inventory is available there. It is a deeper interval. It's slightly gassier. So our perspective is to codevelop the shallower horizons, come back to the Wolfcamp D at a later date, put it into the facilities that would have already been put on, so the CapEx that was spent for the facilities for the co-development, and

then come back in once there's latent capacity and flow the Wolfcamp D into there. So that's another, just a capital efficiency move, rather than trying to codevelop all of the intervals when there's no need with the Wolfcamp D, having so much separation from the Wolfcamp B above.

Oliver Huang

Okay. That's helpful color. And maybe just to kind of follow up to the comments earlier on the Austin Chalk, just wondering, how does the stagger, the two landing zones compare to the development that you all have carried out in the area the last couple of years in South Texas? And are the incremental 65 or so locations primarily coming from that liquids-rich window, or is it pretty ratably spread out across the entire footprint?

Herbert Vogel

Oliver, let me get into that a little bit. On the Austin Chalk, from our first Austin Chalk dedicated well five years ago, we were really working on interval selection. We've really improved on what the best interval was. And then last year and part of the year before, we're really figuring out where is that secondary Austin Chalk zone that optimizes the capital efficiency and the value of each DSU. And so we worked between two different intervals besides the best interval that we had already identified. So what you're seeing now is we've locked in, which is the best way to do that on the stagger. And then in some cases, there's also Eagle Ford. So you can have as many as three landing zones depending on the thickness. We have a bias towards more the liquids-rich oily area. So you'll see great returns, you'll see maybe a few, a little bit lower BOEs in some cases because we'll be in the higher liquids area. But in terms of the returns, they're going to be stronger with the commodity price environment we're looking forward to in 2024. I think that gets to the questions you had there, Oliver.

Oliver Huang

Thanks. I appreciate the color.

Herbert Vogel

You bet.

Operator

Thank you. Our next questions come from the line of Nicholas Pope with Seaport Research. Please proceed with your questions.

Nicholas Pope

Good morning, everyone. I was curious on the Klondike area, you mentioned you drilled a science well, you're running 3D seismic, I guess, what information at this point are you expecting to get from that science? And how that, I think you mentioned you added inventory in Klondike in the

presentation transcript, and I was curious how that might shift with some of the data you get from the science and from the wells that you're expecting to drill through the year.

Herbert Vogel

Okay. Yeah, Nick, a couple of things there, so first of all, you're aware that we have quite a few tools that really help us optimize and get the returns that you're seeing in our wells. So the purpose of the core is really to assess what all intervals we can land in and which is the optimal landing zone even within, there's differences of 10 to 20 feet of where you land can make a difference in the value of the well. So the core has one part, then the logs, so then we have the ability to correlate the core to the logs and apply it to a broader area when we look at the logs and understand what--where the best landing zones are and which intervals we can go for because it can be more than the two that you mentioned up in that area. I'm not going to get into what other intervals might be there, but there's always the possibility of more intervals, and you want to be aware of what those are when you're laying out your development plans.

In terms of the 3D seismic, you're aware, and I've talked about this before, that as you go to the north there, this is more of a, it's a sand play. So this is migrated oil that's there. So you want to have a real good handle on the thickness of the sand intervals that you're targeting and that determines what the economics will be. So that's another development optimization effort on our part. And it's a relatively low-cost data when you look at it, especially compared to some other locations.

Nicholas Pope

And how much well control do you have in that area on your acreage right now? Is there any--what production--is there any--

Herbert Vogel

There's actually quite a bit when we acquired the acreage. There were quite a few vertical wells, and there were several horizontal wells, also. I think if you look at Envers data those wells were around 58 barrels of oil per foot. So that's quite good. And then there's more offset wells in the Dean. I think we're going to be able to optimize from there just based on what we know from all the Dean wells we have over in North Martin, which are 10 miles away.

Nicholas Pope

Got it. That's very helpful. Shifting to the balance sheet. Curious with the notes in '25 and '26, obviously, the '25 is going to come current at some point in the next year. Any thoughts about what the plans are for those two notes, if you might accelerate calling them at some point? How do you all think about that relative to kind of the opportunities that you'll have?

Wade Pursell

Yeah, great question. I mean the '25, as you say, are coming the closest. They'll mature in the middle, mid-2025. It's a rare time where the cash that we have on the balance sheet, that you can

assume that we would pay these off with cash, is earning interest pretty darn close to the coupon. So we're obviously just being flexible with the balance sheet and hanging on to our liquidity.

We'll pay those off, obviously before they mature. I can't tell you when that will be, but it will certainly be before then at some point. And the '26s, they're kind of coming on the radar screen as well. All of our bonds have nice flexibility within them for calling early, and they're already callable with some premium, but they'll be callable at par, I think, beginning in the back half of this year.

Bond market certainly strengthened. I mean, our bonds are certainly trading better than they were. So there's--we'll watch that closely as we always do and try to be opportunistic, and you could see us thinking of a scenario where we might do a new bond that takes out the '26s early, but we'll just be watching all of that as we move through the year.

Nicholas Pope

Got it. That's all I had. I appreciate the time.

Wade Pursell

You bet.

Operator

Thank you. We have reached the end of our question-and-answer session. I would now like to turn the floor back over to Herb Vogel for any closing remarks.

Herbert Vogel

Okay. Thanks, Daryl. So we are well positioned to continue this trajectory to build value and deliver returns going forward. Thank you for your interest, and we look forward to seeing a number of you at upcoming events.

Operator

Thank you. That does conclude today's teleconference. We appreciate your participation. You may disconnect your lines at this time. Enjoy the rest of your day.