



# **The Future of Big Oil**

## **Long-Term Weak Financials Have Accelerated**

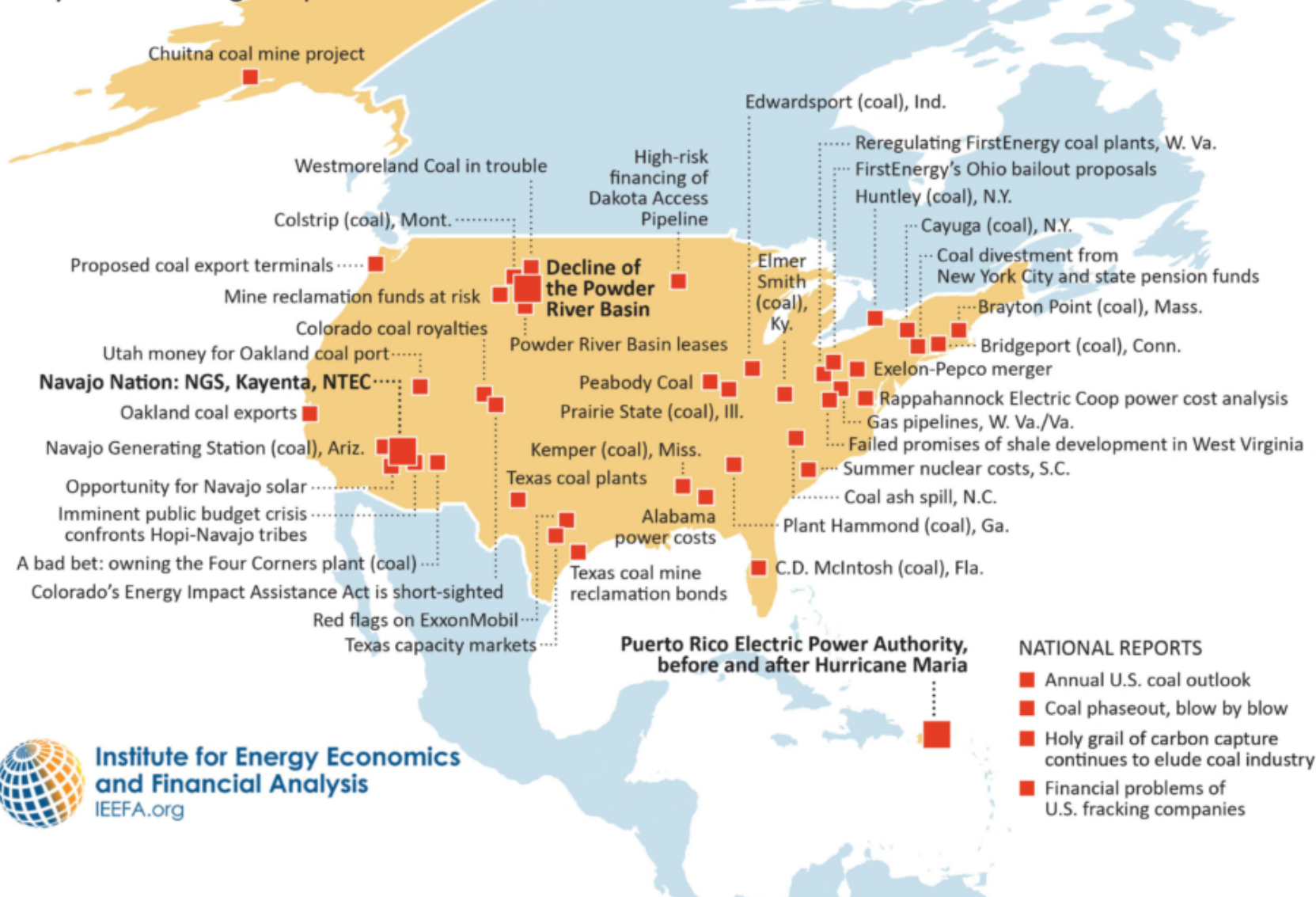
**Kathy Hipple**  
**September 2020**



**Institute for Energy Economics  
and Financial Analysis**  
**IEEFA.org**

# IEEFA has produced more than 200 in-depth reports, including these about the U.S. ...

May 2013 through September 2019



**Institute for Energy Economics  
and Financial Analysis**  
IEEFA.org

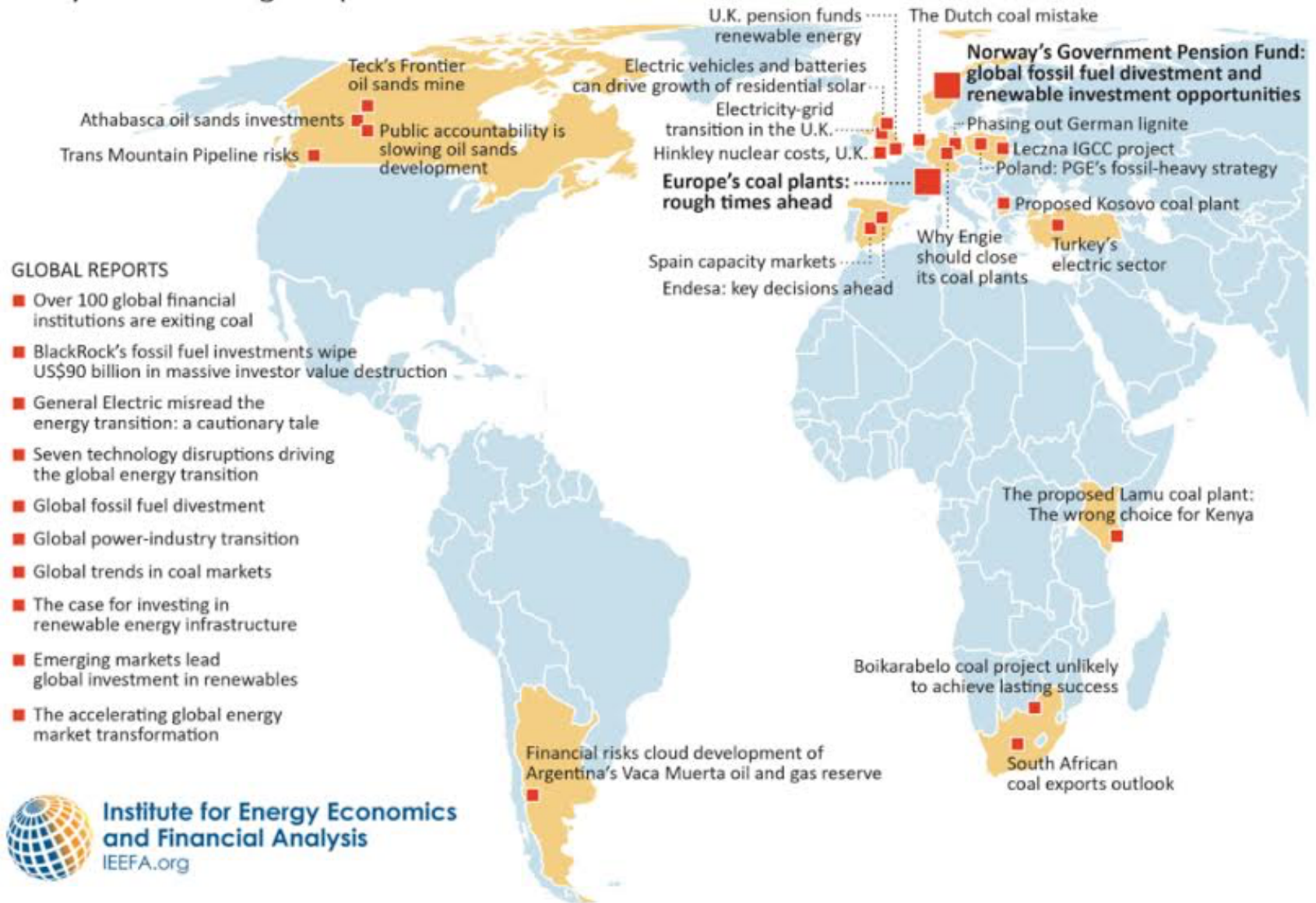
## May 2013 through September 2019





# ... the Americas, Europe, and Africa ...

May 2013 through September 2019

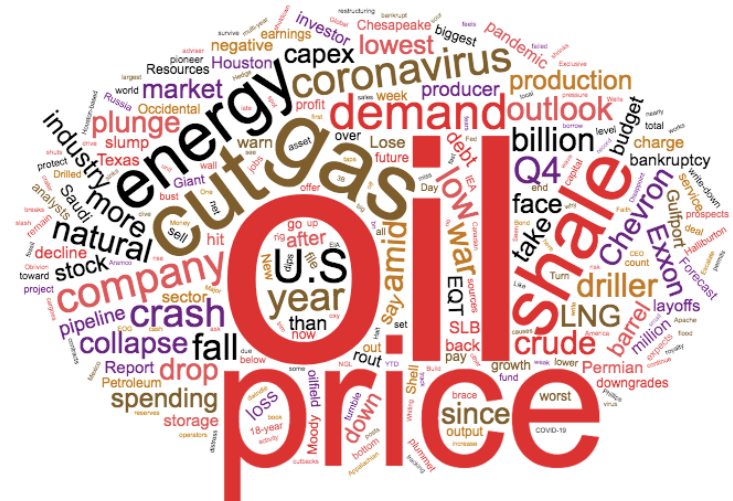


# Overview: Oil and Gas Companies Are Vulnerable, In Long-term Decline

- Oil & Gas companies have underperformed the market for a decade
- Financially, the oil and gas sector has been a bust, despite a production boom
- The energy sector is shrinking
- Today, oil & gas companies are **in extremis**

## In March

- In March, the reality of the economic slowdown brought about by the Coronavirus set in.
- Oil and gas demand forecasts plummeted.
- Then, Russia and Saudi Arabia began an oil price war.
- In short, the world changed.



# The Industry View. . . Or What They'd Like to Believe



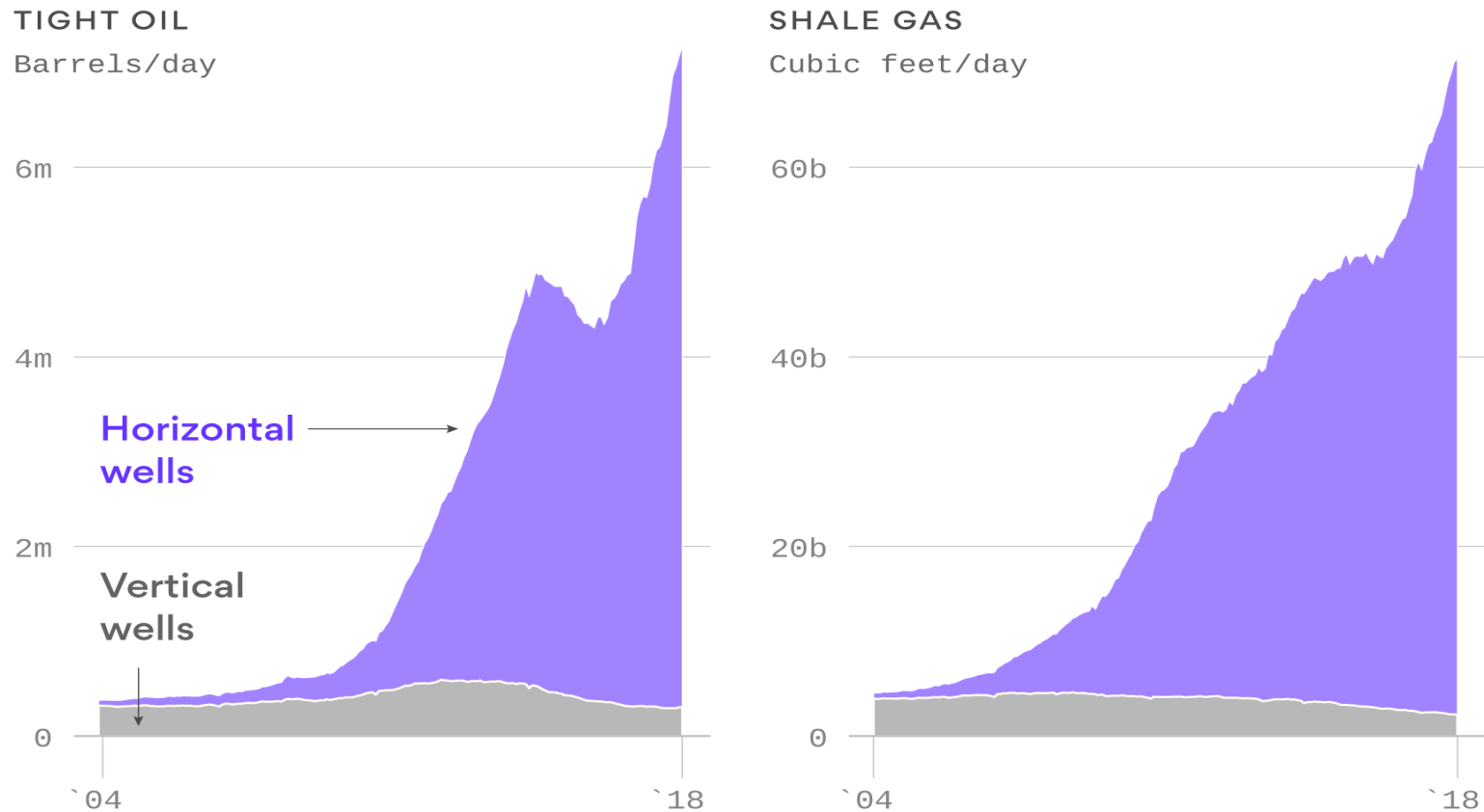
# But The Decline Began Long Ago





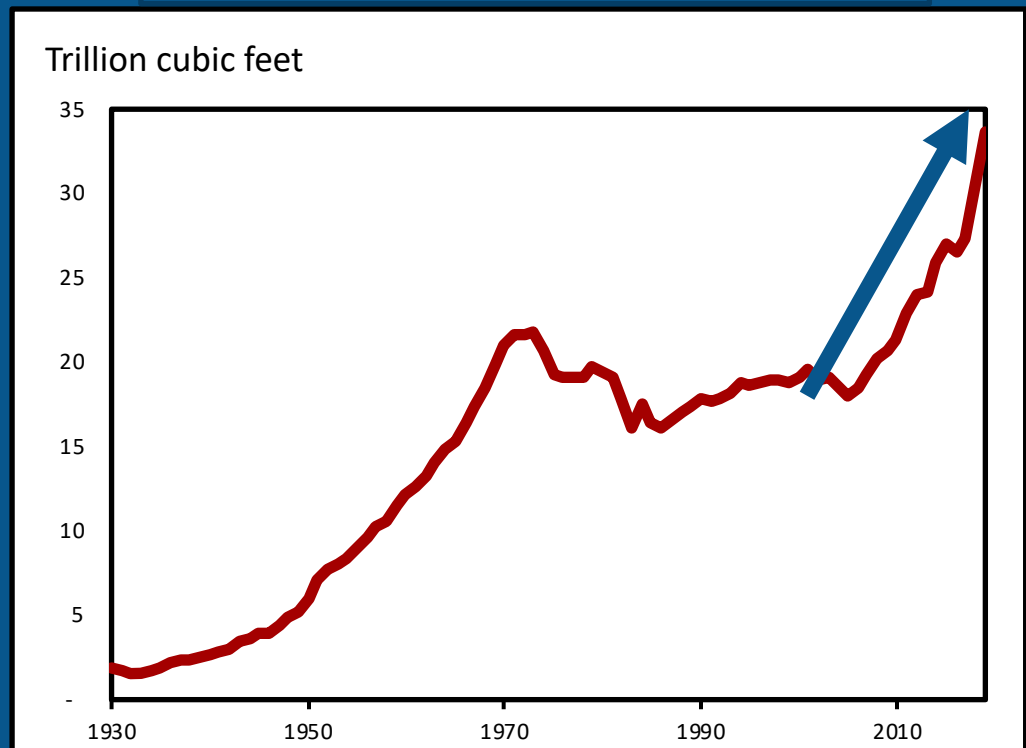
# Horizontal Wells + Fracking Transformed US into World's Largest Oil & Gas Producer.

U.S. tight oil and shale gas production, 2004 to 2018



The “fracking boom” sent U.S. gas production to all-time highs...

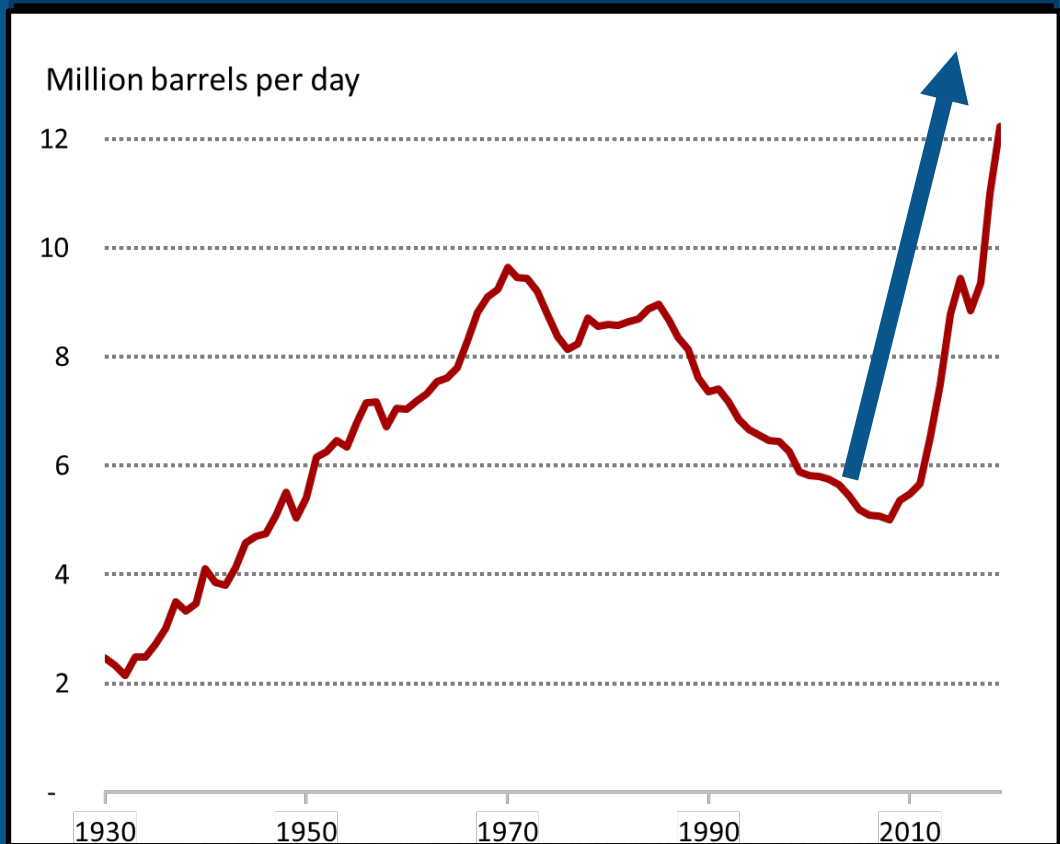
## U.S. Dry Natural Gas Production



Source: U.S. Energy Information Administration

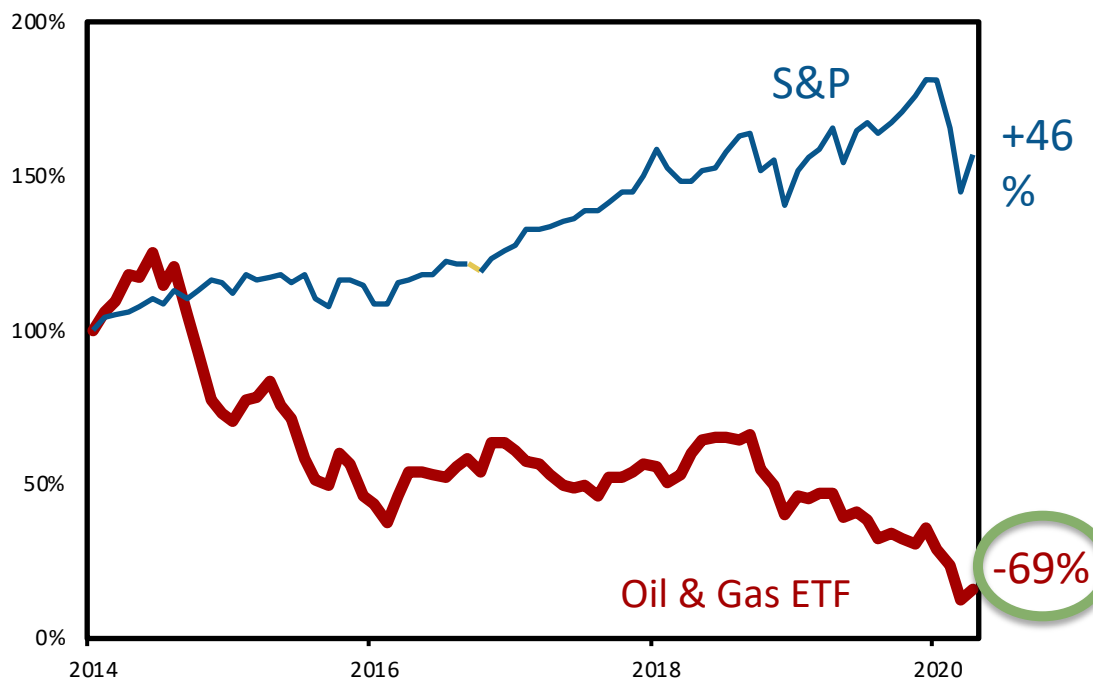
...and propelled  
the U.S. to  
become the  
world's top oil &  
gas producer.

## U.S. Field Production of Crude Oil



Yet, the U.S.  
oil and gas sector  
has performed  
terribly in the  
stock market.

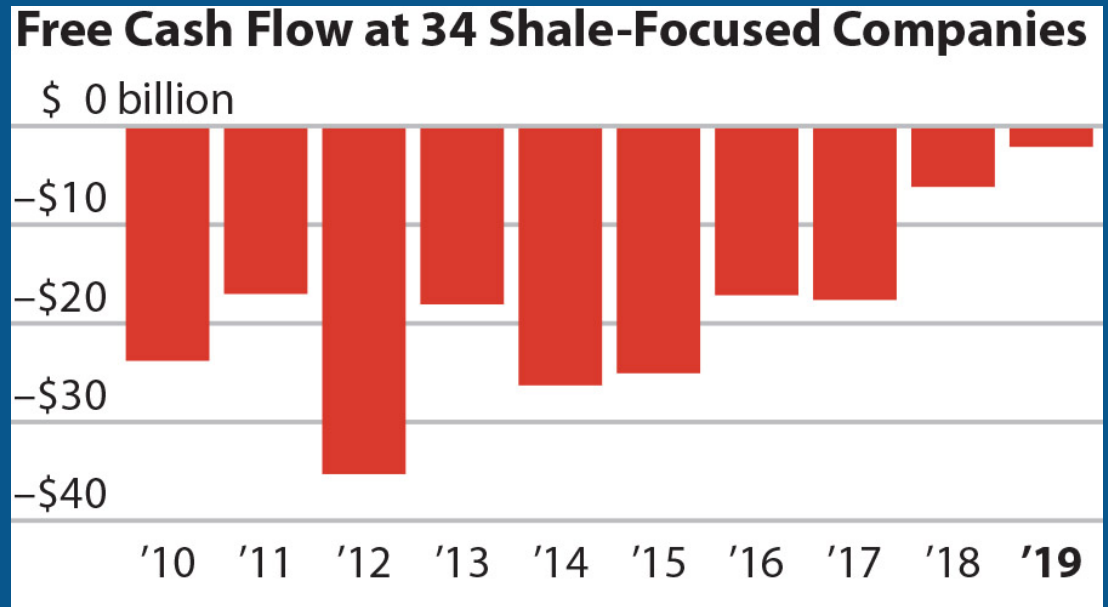
## Stock Market Performance, S&P 500 vs. Oil and Gas



Source: Yahoo Finance, ETF ticker symbol: XOP

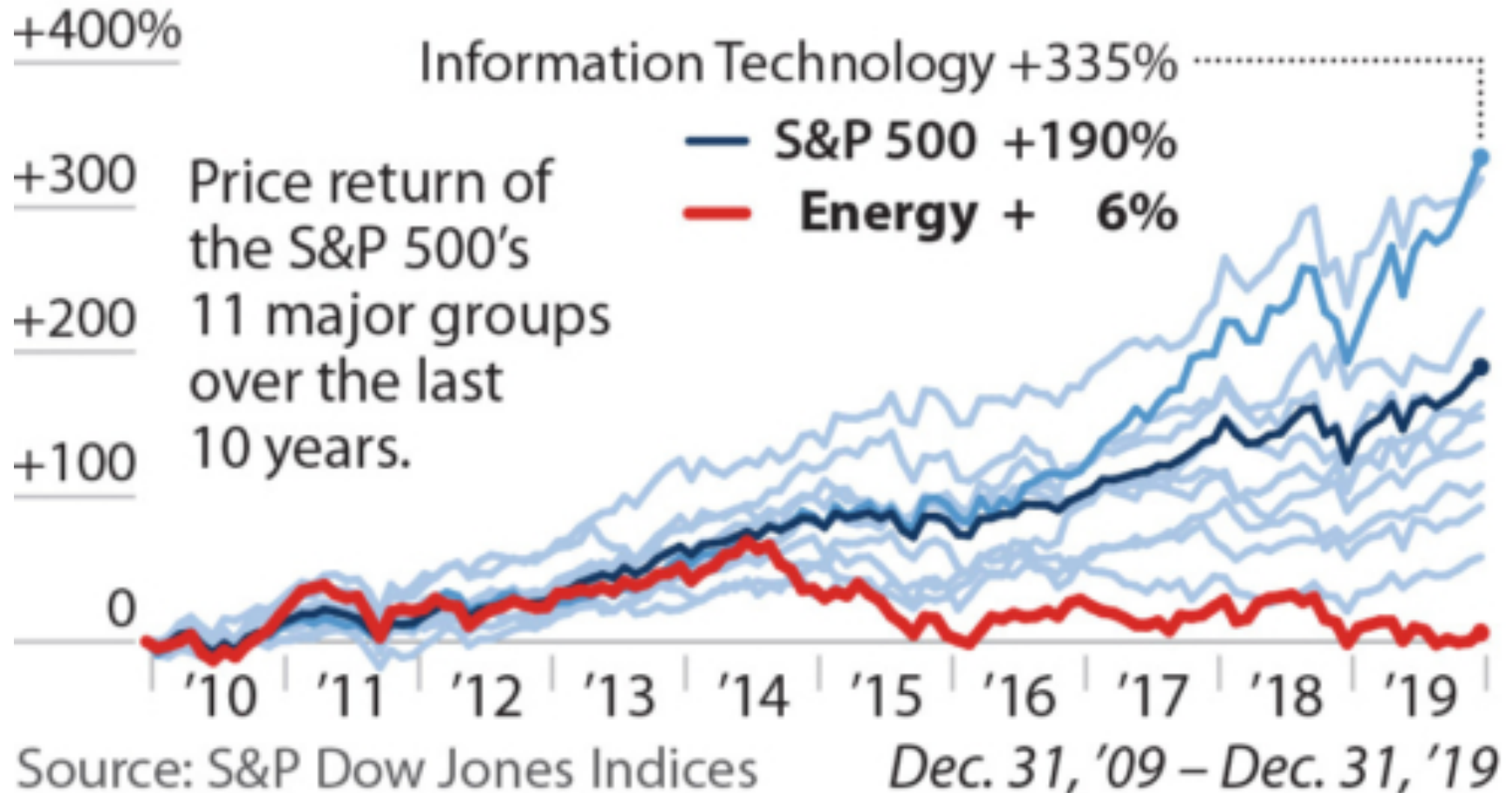
**Fracking has been a financial bust.**

**A deep dive into shale finances reveals a “lost decade” of negative free cash flows.**



Source: IEEFA, from Morningstar and company reports

# Energy: S&P's Worst Sector Over 10 Years

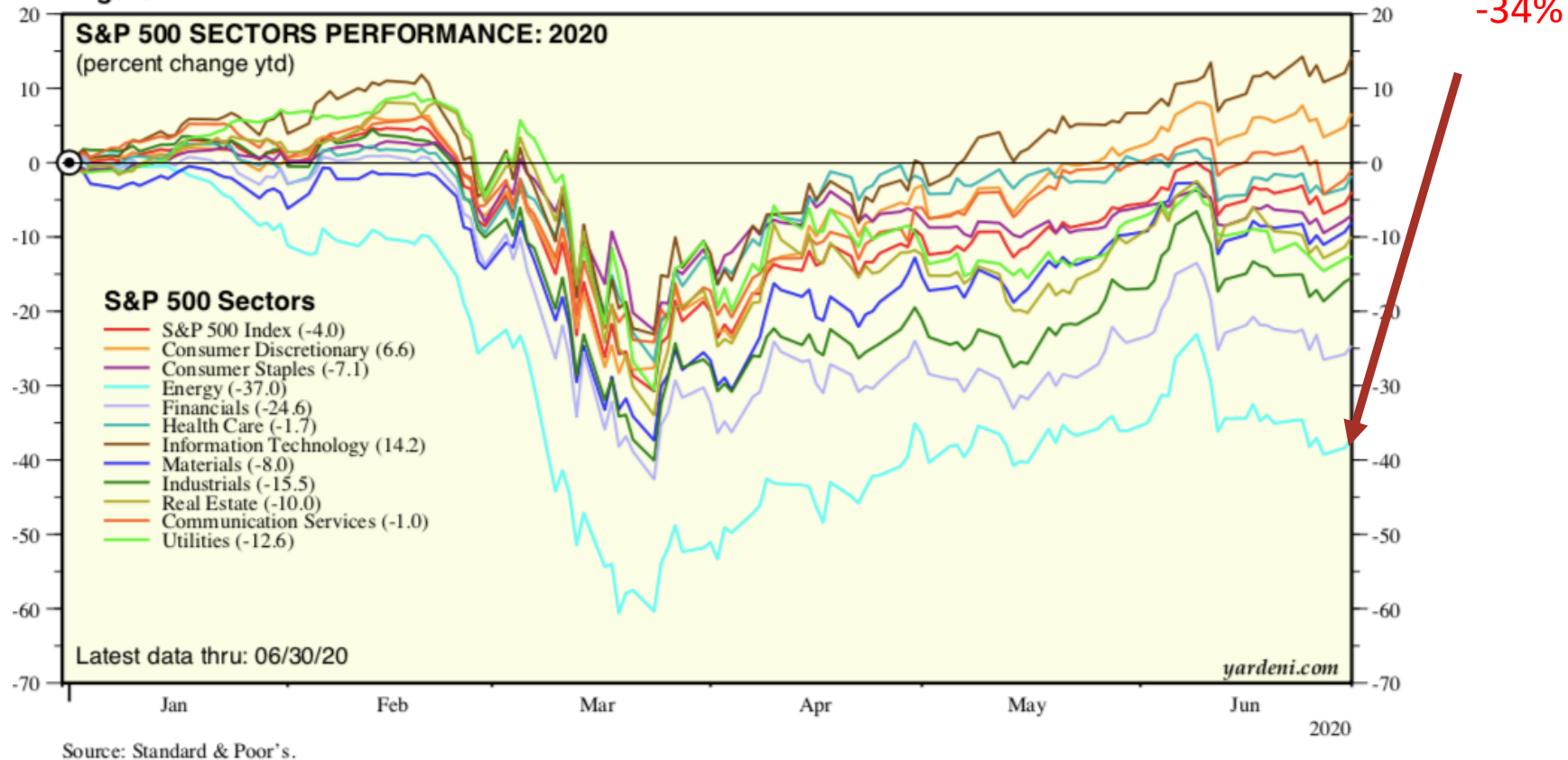




# Energy Sector Declines Further in 2020

## S&P 500 Sectors Performance

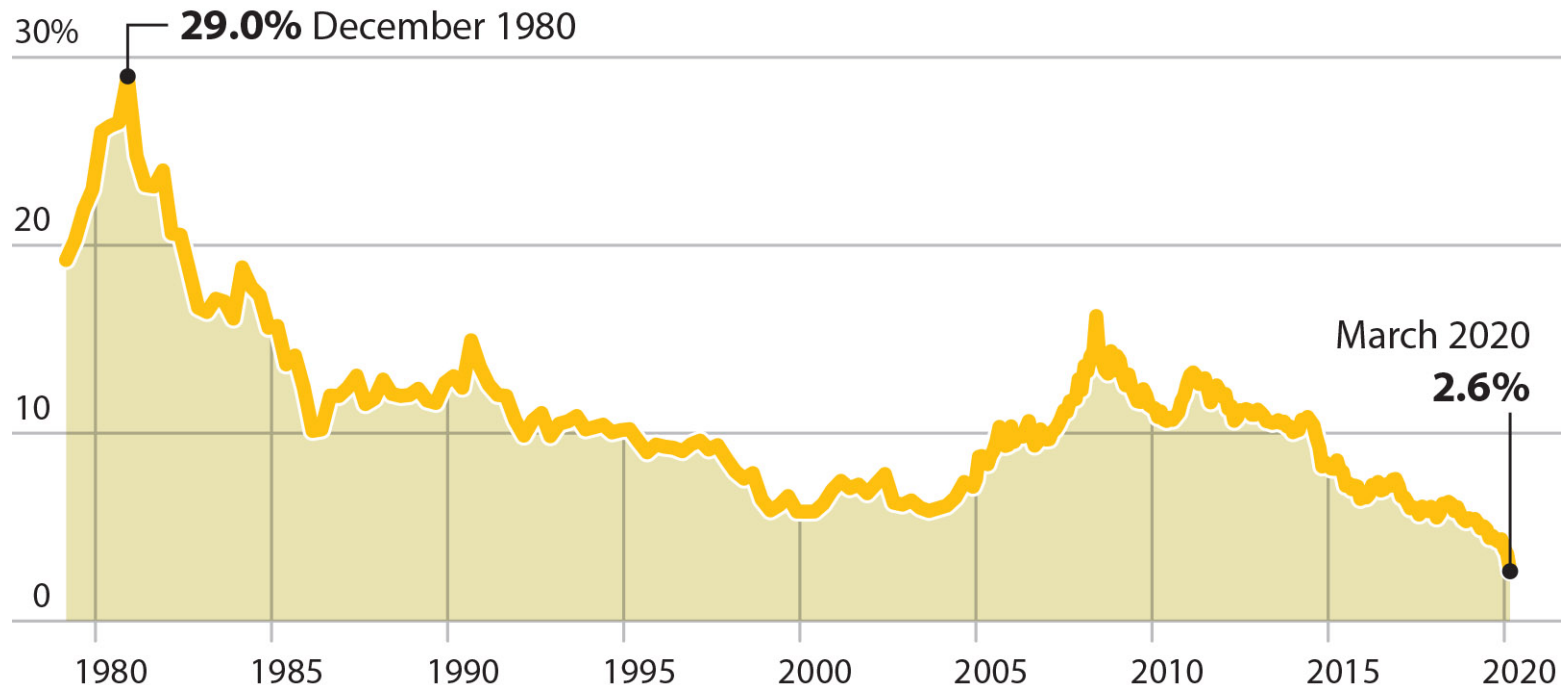
Figure 1.



# Oil and Gas: 2.3% of the S&P 500

## Energy Sector's Vanishing Share of the S&P 500

At the end of 1980, energy companies held 29% of the S&P 500's market value, but have vastly underperformed the rest of the market since then, and had fallen to just 2.6% at the end of March 2020.



Source: Sibilis Research

Based on GICS sector weightings

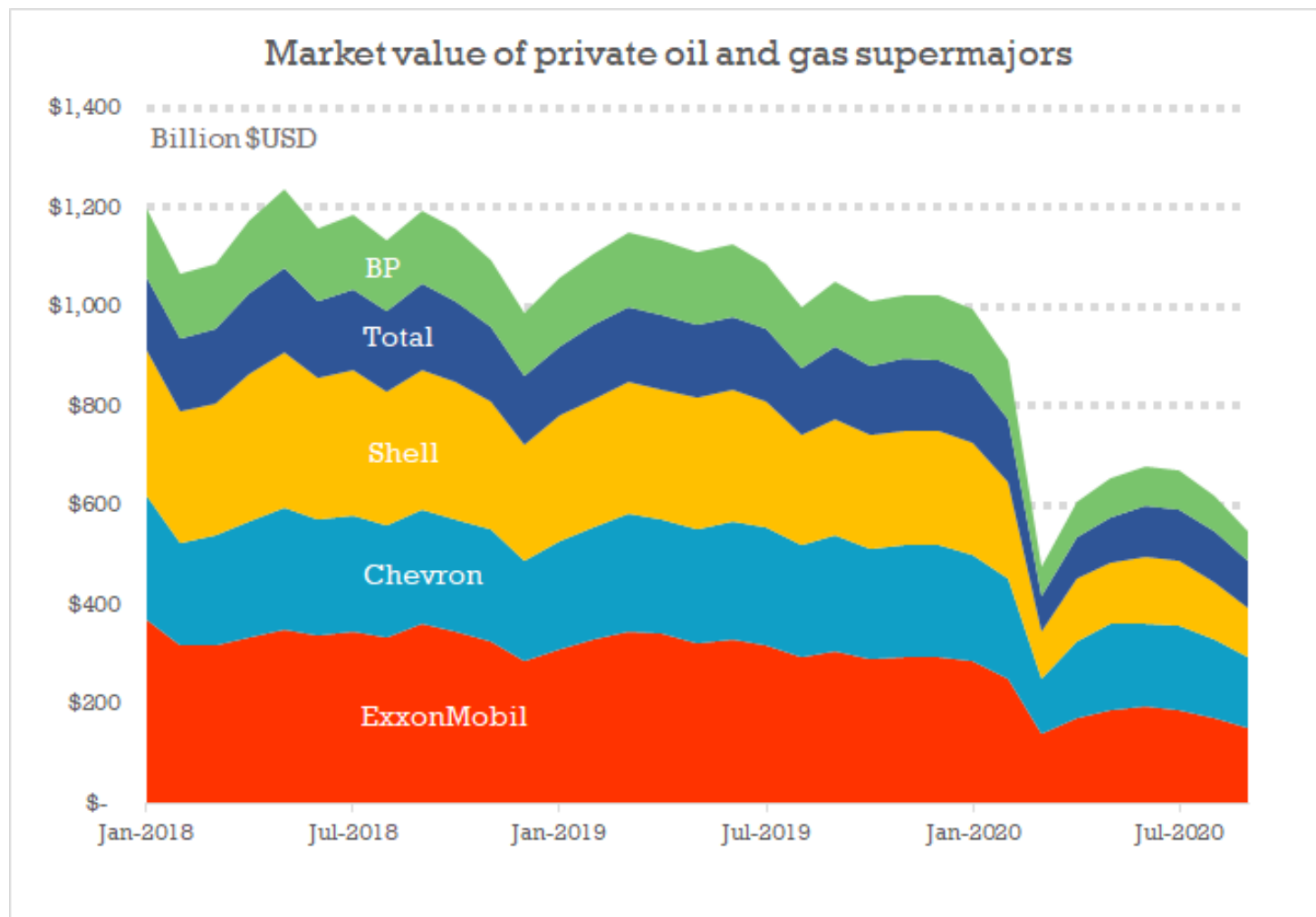
# Energy No Longer Dominates S&P's Top 10 List

	1980	2018
1	IBM	Apple
2	AT&T	Microsoft
3	<b>Exxon</b>	Amazon
4	<b>Standard Oil of Indiana</b>	Facebook
5	<b>Schlumberger</b>	Berkshire Hathaway
6	<b>Shell Oil</b>	JP Morgan
7	<b>Mobil</b>	<b>ExxonMobil</b>
8	<b>Standard Oil of California</b>	Alphabet, Inc. B
9	<b>Atlantic Richfield</b>	Alphabet, Inc. C
10	GE	Johnson & Johnson

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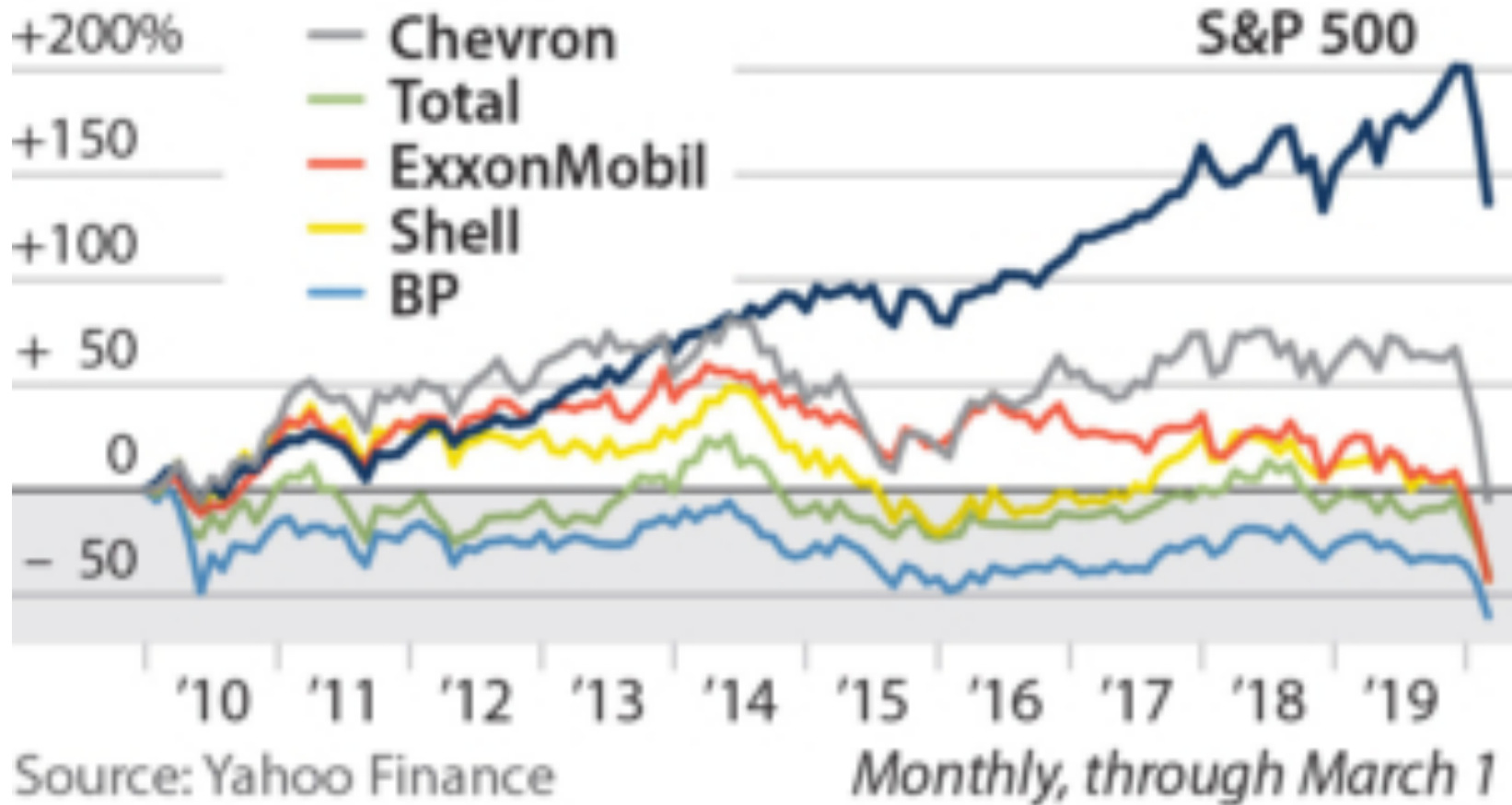
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9	<b>Atlantic Richfield</b>	Johnson & Johnson
10	GE	Proctor & Gamble

# Big Oil is Not So Big



# Despite High Dividends, Oil Majors Underperform

## Performance of Oil Majors vs S&P 500





Oil Majors  
are paying  
(shareholders)  
beyond their  
means...

\$216 billion more  
than their FCFs from  
2010-2019.

## 5 Supermajors: Free Cash Flow, Shareholder Distributions, Cash Deficits, 2010–2019 (in millions)

	Free Cash Flow	Dividends and Buybacks	Deficit	FCF as a Share of Payouts
Exxon-Mobil	\$137,452	\$206,176	(\$68,724)	67%
Chevron	\$48,787	\$93,776	(\$44,989)	52%
Shell	\$104,541	\$131,074	(\$26,533)	80%
BP	\$16,842	\$66,143	(\$49,301)	25%
Total SA	\$32,029	\$58,913	(\$26,884)	54%
Sum, 5 Supermajors	\$339,651	\$556,082	(\$216,431)	61%

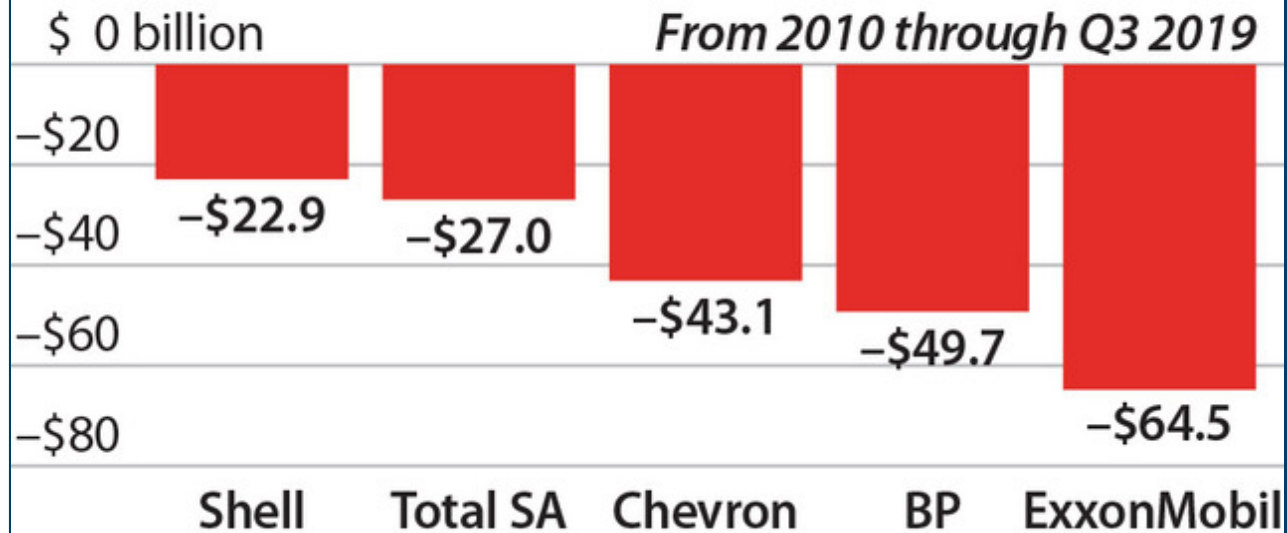
**5 Oil Majors' FCF Didn't Cover  
Dividends/Buybacks Over the Past Decade**

Source: IEEFA, from Morningstar and company reports

**All Oil Majors  
paid out more to  
their shareholders  
than they generated  
from their  
operations**

## Oil Majors Outspending Their Cash Flows

Deficit between free cash flow and shareholder dividends



Source: IEEFA, based on company financial reports

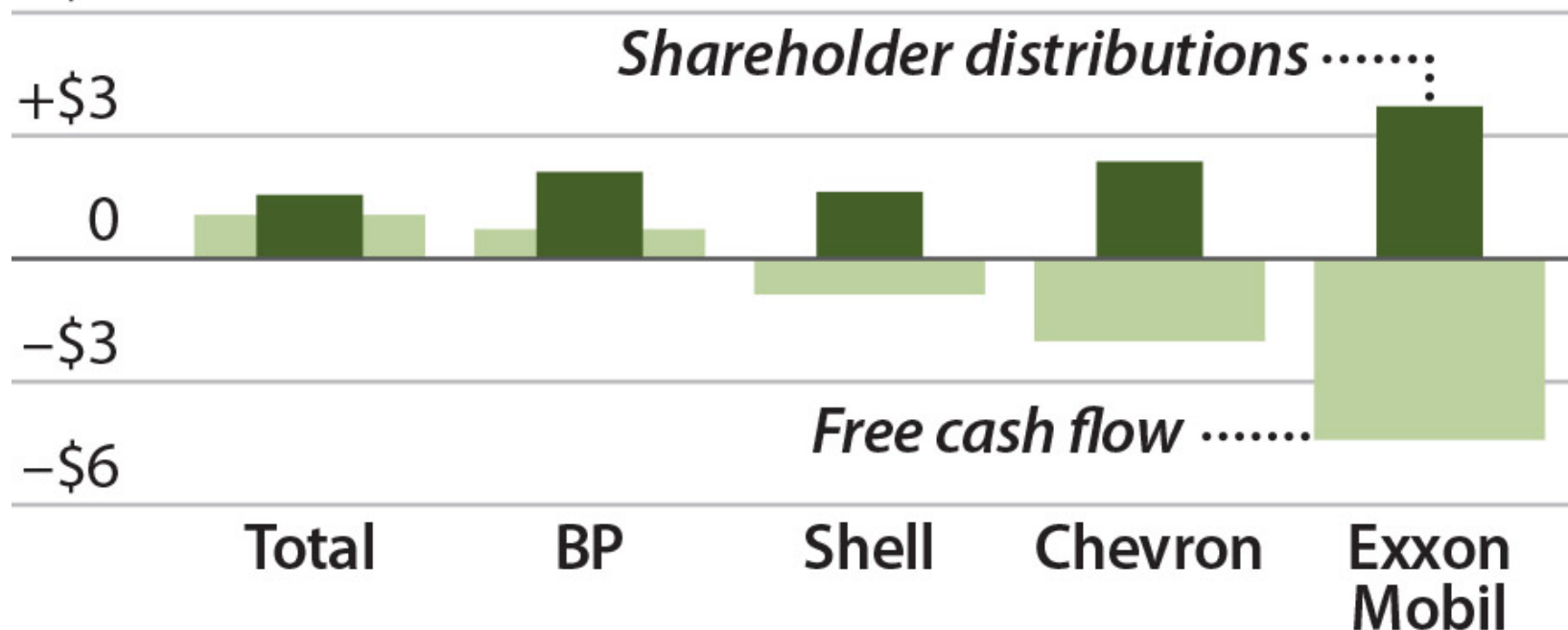
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Source: IEEFA, from Morningstar and company reports

# Oil Majors' Payouts Exceeded Cash Flows in Q2

Free cash flow and shareholder distributions, Q2 2020

+\$6 billion



Source: IEEFA, based on company financial reports

# Oil Majors Face Major Challenges

- Massive write-offs
- Demand forecasts slashed
- Oil and gas glut
- Petrochemicals will not come to the rescue.

## Massive Impairments



\$11.7 billion (Q2)



\$8.1 billion (Q2)



\$16.8 billion (Q2)



\$4.8 billion (Q2)



\$2.9 billion  
(Q1 2020)

Source: Company reports

Oil majors are  
writing off  
massive amounts  
of their assets.

More  
Impairments  
Likely

Oil Giant May Have a HUGE Q4 Write-off



20%

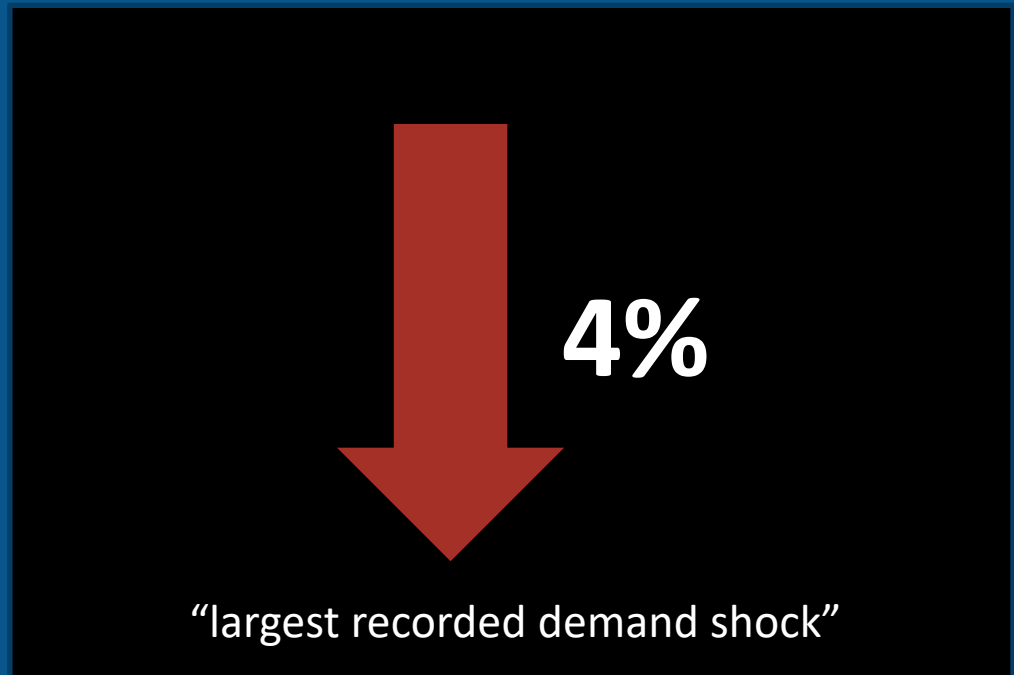


## And Now?

- Oversupply continues
- Demand forecasts cut
- Impairments announced
- Capital Expenditures (capex) cuts
- Debt and equity investors flee

**Demand will experience the “largest recorded demand shock in the history of global natural gas markets.”**

## Global Gas Demand



Source: IEA

**Oil market  
“remains fragile.”**

**“Enormous  
uncertainties.”**

## Global Oil Demand



Source: IEA, others

## Upstream investment plummets

- Below levels in last oil bust
- Flat through 2021

### Capital Expenditures (Capex) Slashed



Source: Rystad, IEA

## What Next?

The oil and gas glut  
will continue.



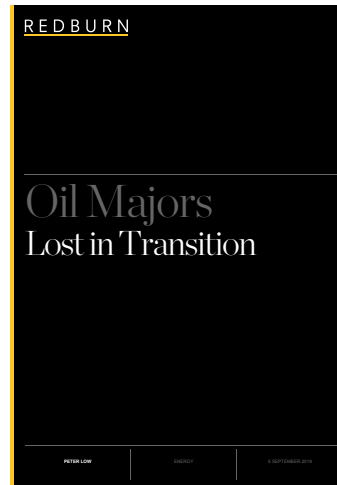
**Oversupply of  
oil and gas  
will put downward  
pressure on  
the sector**

## Conclusion & Implications

- Oversupply continues
- Failing business model
- Ongoing financial distress
- Weak stock returns



## What Next?



“When industries face existential risk, historical multiples provide no floor for share prices.”

--Redburn  
Oil Majors: Lost in Transition

# Oil Majors Were Once in Lockstep



# Oil Majors' Strategies Diverge



## U.S. Oil Majors: ExxonMobil

### Double Down on Oil & Gas

The Exxon logo, featuring the word "Exxon" in a bold, red, sans-serif font. The two 'x's are stylized, with the second 'x' having a longer, more pronounced rightward stroke.

“Despite the challenging environment, the Corporation’s view of long-term supply and demand fundamentals has not changed significantly.”

Source: Exxon Q2 10Q

## U.S. Oil Majors:

### Double Down on Oil & Gas



Source: Chevron

## European Oil Majors

### Small steps. . . .




- Plans to become carbon-neutral energy business by 2050
- Restructuring
- Cut up to 40% in operating costs and capital spending on new projects in its upstream segment.
- Integrated gas division, which includes LNG operations and gas production, is expected to see deep cuts.
- Implement layoffs and eliminate management layers.

Source: Reuters

## European Oil Majors

### . . . . And Big Steps

- "BP is setting out the most significant pivot as yet among the majors, most i by cutting target production 
- Net zero by 2050
- Buying into offshore wind
- Plans to increase annual low carbon investment to around \$5 billion a year by 2030

Source: UBS

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