



A story of impairments: Themes from the Oil Majors' Q2 2020 earning calls

Second quarter earnings of the oil and gas majors reflected the full impact of lockdowns introduced in many countries to stem the spread of COVID-19. Companies indicated that they had seen some early signs of demand recovery but cautioned that they were not planning for a rapid rebound in economic activity. Several companies commented on the positive contribution to earnings made by their trading businesses, which was underpinned by high price volatility. These companies stressed the benefits of their integrated business models in generating value across oil, gas and power trading.

Revisions to price assumptions

Some of the oil companies reported impairments across their portfolios in the second quarter, which to a large extent reflected downward revisions to long-term price assumptions for oil and gas and, in some instances, also refining margins. Analysts questioned companies on the frameworks they had used to calculate impairment charges. The analysts also sought guidance on whether companies were likely to impair any assets in the third quarter.

Maintaining capital discipline

Most companies referred to the flexibility they possess to further reduce capital expenditure if the economic recovery is weak. Some analysts were interested in the impact on production in 2021 due to the lower level of capital expenditure this

year. Companies said there would be some impact on volumes but reiterated their pursuit of value over volume. Analysts also wanted to understand companies' priorities for cash and asked if they would favour reinstating or preserving the dividend over raising capital spending.

Shareholder distributions in focus

Analysts asked for companies' views on the sustainability of their progressive shareholder remuneration policies in the medium-term. Analysts also asked if dividend policies were being reviewed due to the uncertain macro outlook. A couple of companies announced a new shareholder distribution policy during second quarter earnings calls. Analysts enquired about the rationale for changing the dividend policy.

Chemicals market dynamics

Analysts requested insights on the current demand dynamics in the chemicals sector and views on the longer-term prospects for the sector. Companies noted that COVID-19 had a significant impact on durables in the automotive and construction sectors, resulting in overall reduced volumes. However, this was partially offset by resilient demand for products going into the packaging and hygiene segments.

Renewables and hydrogen in the energy transition

Analysts raised several questions around the energy transition that were largely focused on two enablers: renewable power generation; and the prospects for hydrogen. Around a third of the questions on the energy transition related to renewables. This included questions to companies around the scale of their installed or planned renewable power capacity and the rate of growth in their electricity customer base. A further third of questions centered on companies' views of the role of hydrogen in the energy transition. Companies were also asked about the economics of their announced hydrogen projects and the regulatory framework that may be needed to support some of these investments.

The oil companies said that hydrogen would be a long-term play and that they would scale up their investment over time. They added that, at least in the short-term, blue hydrogen will be more cost competitive than green hydrogen and will help to decarbonize natural gas. The remainder of the energy transition

questions explored capital allocation to low carbon businesses, the visibility on the returns from low carbon projects and the balance between organic growth versus M&A. Companies advised that they intended to provide more colour around their low carbon business plans at strategy updates for investors scheduled for later in the year.

Brunswick Group

16 Lincoln's Inn Fields
London WC2A 3ED
United Kingdom

Simon Maine

smaine@brunswickgroup.com
+442073963531

Will Medvei

wmedvei@brunswickgroup.com
+44 (0) 7823 527148

Patrick Handley

phandley@brunswickgroup.com
+44 7974 982395