



**Institute for Energy Economics
and Financial Analysis**

Energy Sector Ends 2023 With a Weak Comeback and a Negative Outlook

Tom Sanzillo, Director of Financial Analysis

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Key Findings

The oil and gas sector comeback ends near the bottom of the stock market.

The \$70 to \$80 per barrel oil prices in 2023 could not match 2022's war-driven spike of \$125 per barrel.

Tighter scrutiny for debt markets puts climate promises by the energy sector to the test.



Executive Summary

At the end of 2022 and into the first quarter of 2023,¹ great news for the energy sector was reported with enthusiasm. When 2022 record profits were announced in February 2023, the message was clear that the failure for most of the last decade was a thing of the past.² There were banner headlines of a comeback.³

During 2023 the message was underscored with reports of a new capital discipline—lower drilling and higher dividends.^{4,5} And, the comeback grew larger with Exxon’s \$60 billion announced acquisition of Pioneer Natural Resources.⁶ Although there were indications of a cooling-off in production,⁷ the “oil is back” mantra continued throughout 2023.

The oil and gas industry claimed 2023 was a resounding success.⁸ It lifted the United States to a 21% market share, No. 1 among the world’s oil and gas producers. The United States pulled far ahead of Saudi Arabia (a 13% market share) and Russia (10%). One bullish analysis suggested the sector would dominate in 2024.⁹

Despite the good news, however, the energy sector struggled. In February—when headlines touted the success of the industry—the oil and gas sector actually was near the bottom of the stock market (Figure I). The fact that the energy sector was sparring with the utilities and financial sector for last place in the market was totally overlooked. Frackers, later joined by the oil majors, managed to drag the sector down for the rest of the year.

¹ Houston Chronicle. [With record profits and rising stock prices, the oil industry has its swagger back—at least for now.](#) November 21, 2022.

² Financial News Media. [Oil-gas industry earned record profits in 2022 as momentum is expected to continue for 2023.](#) February 22, 2023.

³ CNBC. [Oil companies made \\$200 billion in profits in 2022. Here’s how.](#) March 3, 2023. Also see: Reuters. [Big oil doubles profits in blockbuster 2022.](#) February 8, 2023.

⁴ New York Times. [It’s not just Willow: oil and gas projects are back in a big way.](#) April 6, 2023. Also see: Gilmore. [Big oil: Why manufacturing companies value capital discipline.](#) June 6, 2023.

⁵ NPR. [America is going through an oil boom—and this time it’s different.](#) June 9, 2023.

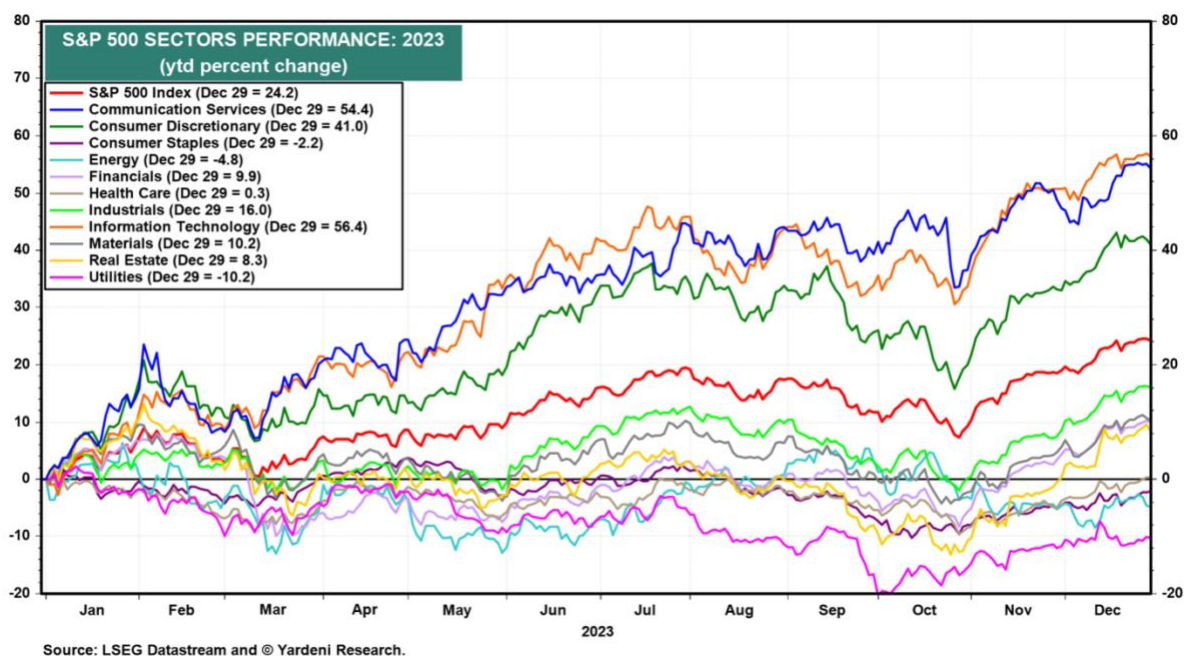
⁶ CNBC. [US oil is back, and Exxon’s \\$60 billion deal isn’t even the biggest signal.](#) October 15, 2023.

⁷ Reuters. [US Oil gas production net production set for turn down later in 2023.](#) July 5, 2023.

⁸ Forbes. [The US domestic oil industry closes a remarkably strong 2023.](#) December 31, 2023.

⁹ Motley Fool. [This stock market sector could dominate in 2024. Here’s why.](#) December 18, 2023.

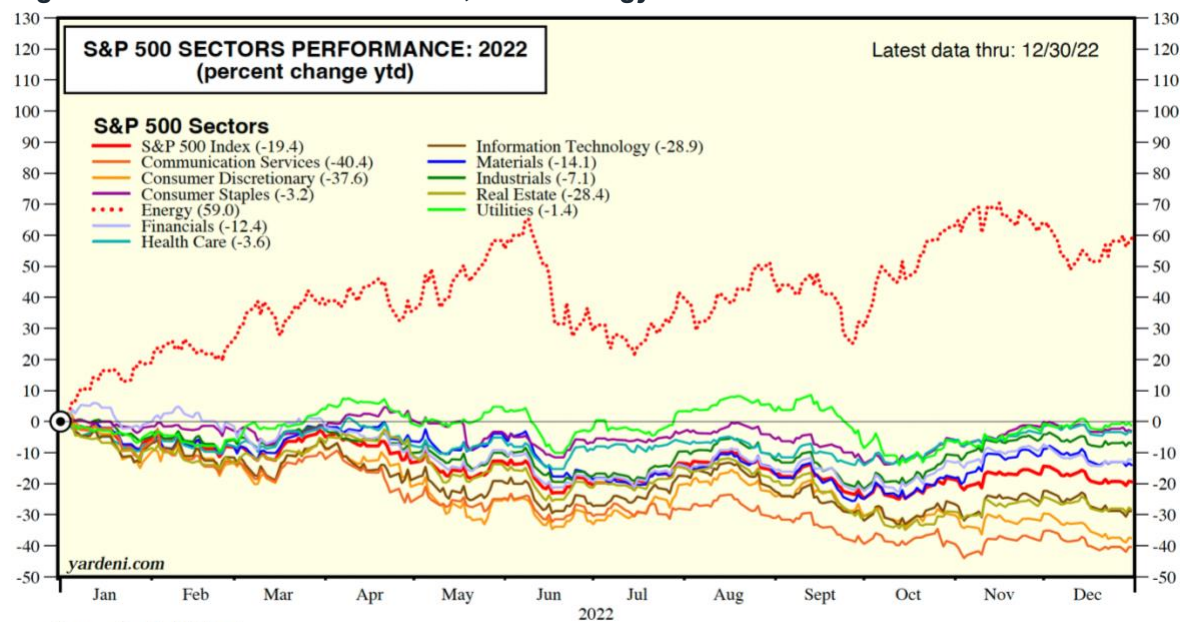
Figure 1: S&P 500 Sector Performance, 2023; Energy Places 11th Among 12 Sectors



But is there hope for the industry's future?

Dividends have obscured the fundamental explanation for the industry's stock failings. The Ukraine invasion catapulted the price of oil from a post-COVID-19 recovery price of \$100 per barrel to \$125 per barrel. A review of 2022 prices shows why the bluster may have been merited, since the industry was No. 1 in the stock market for the whole year as oil prices soared. At the same time, the world's economy faltered and the market lost value (Figure II). Against the backdrop of an otherwise decade of poor stock performance, the Ukraine-driven price spike actually spoke to the speculative nature of the energy sector today and its negative outlook, rather than the blue-chip performance of the past.

Figure 2: S&P Sector Performance, 2022: Energy Sector Leads the Market

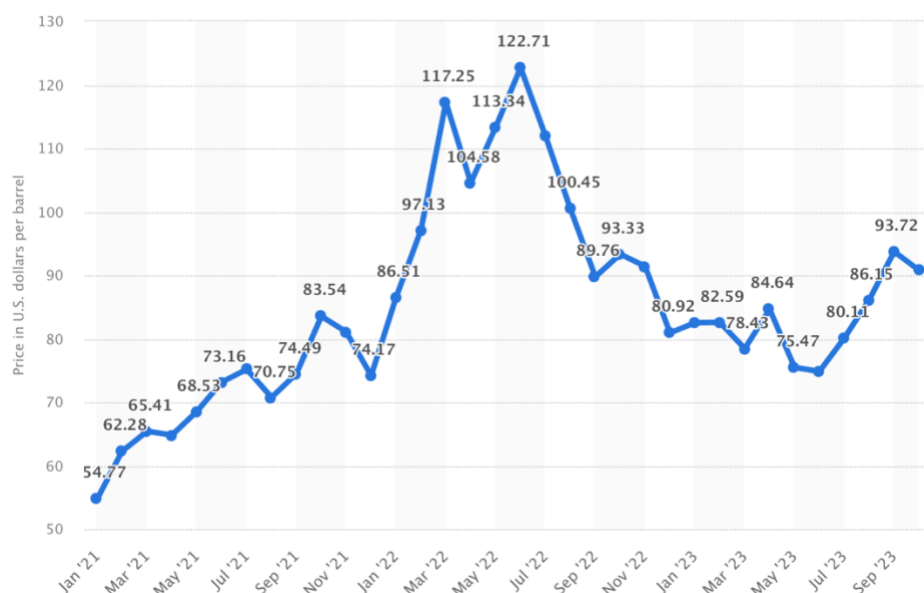


The price of oil almost tells us the full story of the industry. In 2021, Brent crude averaged \$70.89 per barrel. It rose to \$100.94 in 2022 before falling back to \$82.40 last year.¹⁰ From 2016 through 2020, the average oil price was \$62.69,¹¹ and the industry lagged the market in four of the five years. The Ukraine bump and subsequent economic events have kept oil prices high relative to the 2016-20 period. Even with prices in the \$80 range, however, the industry bounced around at the bottom of the broader market, which increased by 24%.

It appears that the energy sector needs oil prices north of \$100 per barrel to achieve the kind of financial performance for which it had previously been known. Such oil prices, however, now appear to ensure weak economic growth.

¹⁰ EIA. [Short-term energy outlook](#). December 12, 2023.

¹¹ EIA. [U.S. Crude Oil First Purchase price](#). Last visited January 9, 2024.

Figure 3: Oil Price From January 2021 to September 2023

Source: [Statista](#).

The markets can expect a 2023 end-of-year earnings call season that reflects the lower prices. For example, 2023 third-quarter profits for Exxon were half of the results reported in the third quarter of 2022.¹²

The fortunes of the energy sector are no longer linked to general economic growth. The energy sector's fate is linked closely to the price of oil, which is determined by a combination of supply-and-demand factors and the legitimacy crises that plague large producer states.

For the energy sector to sit in next-to-last place—reporting a 4.8% loss during a period of relatively high oil prices and a rising broader market—is a sign that something is wrong.

Other market watchers are not optimistic. Moody's Investors Service, Fitch Ratings, and Standard and Poor's each released new, stepped-up analytics on climate change.^{13,14,15} If applied to today's energy sector, Fitch's new climate paradigm would probably result in a significant number of downgrades.¹⁶ The credit agencies, stung by criticism on their failure to flag the 2007-09 mortgage meltdown, are raising red flags: Fossil fuel companies are increasingly risky enterprises, and most are ill-prepared to meet future challenges.

¹² ExxonMobil. [ExxonMobil announces third quarter 2023 results](#). October 27, 2023.

¹³ Moody's. [Climate risk is business risk](#). Accessed January 8, 2024.

¹⁴ Fitch Ratings. [Over half of corporates facing climate-related downgrades by 2035 are investment grade](#). October 24, 2023.

¹⁵ Reuters. [Large companies' assets growing risk of climate impact—S&P Global](#). September 15, 2022.

¹⁶ Fitch Ratings. [op. cit.](#)

Companies in the sector have made promises to shareholders and the public to address climate change. The actions by credit agencies are telling the companies that their plans (announced with celebratory press releases) now must meet serious credit standards. Are the new businesses being planned capable of producing revenue that can sustain necessary debt levels? Are companies integrating the planned changes into their corporate portfolios, organizational plans and technological makeup? Are the new technologies proposed by the energy sector competitive with companies offering sustainable alternatives? Do the new businesses raise environmental or social issues that should be addressed? Are there clear and realistic steps to get from the current designs of energy sector companies to their newly minted aspirational, climate-friendly ones?

The accolades that many business analysts have lavished on the energy sector are usually based on production. They are short-term and cash-driven, when they are related to financial performance at all.

The energy transition applause is also extended to technologies that have not yet met technological standards. Such promises, like carbon capture and sequestration, can only be fulfilled if supported by permanent subsidies that maintain the quasi-monopoly status of coal, oil and gas.^{17,18,19} While the stock traders are citing cash surpluses as the measure of energy sector success, they have ignored the fact that the current source of cash is based on a major disruption caused by Russia's invasion of Ukraine. The invasion created a price spike and, with it, a cash surplus—hardly the basis for a robust credit rating.

Typically, oil and gas companies use cash surpluses to clean up the balance sheet (lower debt), provide shareholders with additional benefits, and invest in future projects. In the past, surpluses were spent on new reserves that could ensure a robust flow of oil and gas. But the market penetration of alternatives to fossil fuels in each sector (power generation, transport and petrochemicals) is growing. The International Energy Agency and others are warning that aggressive reserve replacement is not the asset-building, credit-positive strategy of the past.

The traditional fossil fuel business model no longer works. Credit rating agencies and other long-term investors tend to support standalone financial performance (positive cash flows from capital investments) demonstrated over a period of time under varying business cycles. To the degree policy considerations are integral to a business model, the regulatory and political environment is assessed.

Institutional investors under the spell of advisors with short-term, fee-driven contracts, fossil fuel lobbyists, and overwhelmed fund management staff are loath to take action to protect fund values from the industry's negative outlook as long as the short-term dividends arrive. But while most are

¹⁷ IEEFA. [CCS: An unproven technology that cannot meet the world's mitigation needs.](#)

¹⁸ M. Bui, *et al.* [Carbon Capture and Sequestration: The way forward.](#) *Energy & Environmental Science* (Journal of the Royal Society of Chemistry) 11:1062-1175. 2018.

¹⁹ For a discussion of how United States policy supported the coal industry as a protected political class through long-term policy mobilization, see: Daniel Yergin. *The Quest* (New York: Penguin, 2008), p. 400.

dismissing their long-term fiduciary obligations, some longer-term investors are looking beyond fossil fuels. Many have gone the route of investor engagement and now are reevaluating their exclusion list standards, or moving capital into indexes and investments with less or no fossil fuel exposure.^{20,21}

What we are watching for:

1. **The price of oil.** The trend in which geopolitical events drive oil and gas prices is likely to continue. We expect disruptions of this nature to become more frequent but steeped in appeals to societal division. As the financial viability of oil and gas erodes, the industry will exercise its direct state power or quasi-monopolistic power to boost its position and stave off energy transition. At what cost and for whom?
2. **Growth in reliance on low- or no-carbon indexes.** It is becoming abundantly clear to money managers and their clients that solid returns, low fees and lower emission investments can be found among the rising number of climate-friendly market offerings. All the largest names in the industry now offer these products because customers are demanding them.²² One advisor to several funds considering divestment put it this way: “Over time, we expect low carbon indexes to more closely resemble the carbon exposure of the underlying market cap weighted benchmark as the world moves towards a low-carbon economy.”²³
3. **Market share erosion.** The coal, oil and gas industries face market share erosion in the power sector. There are similar cracks in the relationships between fossil fuel interests and the transport and petrochemical sectors. Every kilowatt-hour of renewable electricity, metric ton of non-fossil feedstock, and electric vehicle sale provides the upside to the downside experienced by the energy sector as its market share erodes.
4. **Technological development.** New technologies offered by the energy sector and its competitors face critical tests of technological and commercial viability. How that viability is achieved—and the role government will play—is essential to understand.
5. **Growing policy consensus away from fossil fuels.** We expect to see a policy consensus around the Paris Agreement and related initiatives, as well as the United Nations plastic accord to move away from fossil fuels. Independent initiatives, like the Fossil Fuel Non-Proliferation Treaty organized by a growing group of stakeholders seeking to fill significant policy gaps in the climate debate, can also be expected to gain momentum.²⁴
6. **Credit Agency Posture:** Do the credit rating agencies turn their substantial database and creditworthiness analytics into a robust tool that can chart new capital market directions?

²⁰ Networks such as Invest Divest, Urgewald and Reclaim Finance offer a variety of tools and information on the design, construction and implementation of exclusion criteria and exit strategies.

²¹ Organizations are forming, like that spearheaded by CERES, to elevate the path that institutional and other investors can follow to safely invest in new technologies and companies.

²² As You Sow. [Fossil-free funds](#).

²³ Vermont Pension Investment Committee. [Climate Risk Divestment Discussion](#). February 2017, p. 8.

²⁴ See for example the [Fossil Fuel Non-Proliferation Treaty](#). Last visited January 11, 2024.

The warning from the poor stock performance and the voices of credit raters to investors is largely negative, and cash surpluses driven by geopolitical disruptions only go so far. This year will begin to see which promises made will be kept.

About IEEFA

The Institute for Energy Economics and Financial Analysis (IEEFA) examines issues related to energy markets, trends and policies. The Institute's mission is to accelerate the transition to a diverse, sustainable and profitable energy economy. www.ieefa.org

About the Author

Tom Sanzillo

Tom Sanzillo, director of financial analysis for IEEFA, is the author of numerous studies on the oil, gas, petrochemical and coal sectors in the U.S. and internationally, including company and credit analyses, facility development, oil and gas reserves, stock and commodity market analysis and public and private financial structures. Sanzillo has experience in public policy and has testified as an expert witness, taught energy industry finance and is quoted frequently in the media. He has 17 years of experience with the City and the State of New York in senior financial and policy management positions. As the first deputy comptroller for the State of New York Sanzillo oversaw the finances of 1,300 units of local government, the annual management of 44,000 government contracts, and over \$200 billion in state and local municipal bond programs as well as a \$156 billion global pension fund.

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