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In Q1, Four of Five Oil Majors Paid More Cash to Investors Than They Made From Operations

Weak Cash Flows Forced Oil Majors to Find Other Means to Fund Shareholder Distributions

Four of the world's five largest private-sector oil and gas companies paid more to their shareholders in the first quarter of 2020 than they generated from their core business operations.

Two of the oil supermajors, BP and Total, reported negative free cash flows in the quarter. BP spent $2.8 billion more on capital projects during Q1 than it generated from selling oil, gas, and refined products, yet still paid $2.9 billion to its shareholders—leading to a $5.7 billion cash deficit for the quarter. Similarly, French oil giant Total posted negative free cash flows of $1.1 billion in Q1, while paying shareholders $2.5 billion, yielding a deficit of $3.6 billion.

Chevron generated $1.6 billion in positive free cash flows during the quarter, but paid shareholders $4.0 billion in dividends and share buybacks, resulting in a $2.4 billion cash deficit. And ExxonMobil produced just $329 million in free cash flows, also making $4.0 billion in cash payments to shareholders, for a $3.7 billion deficit. Only Royal Dutch Shell spent within its means, generating $10.6 billion in free cash flows during the quarter, while paying $5.2 billion in dividend payments and share buybacks.[1] (See Table 1.)

Table 1: Five Oil and Gas Supermajors- Free Cash Flow, Shareholder Distributions, and Cash Deficits, Q1 2020 (Million $USD)

	Free Cash Flow	Dividends and Buybacks	Surplus (Deficit)
ExxonMobil	$329	$4,024	($3,695)
Chevron	$1,589	$3,975	($2,386)
Shell	$10,588	$5,151	$5,437
BP	($2,846)	$2,878	($5,724)
Total SA	($1,065)	$2,491	($3,556)
Sum, 5 Supermajors	***$8,595***	***$18,519***	***($9,924)***

Source: IEEFA, based on company financial reports.

[1] See Sources and Methods for methodology.

The four supermajors with deficits relied on other sources of cash—including borrowing, asset sales, and drawdowns of cash reserves—to sustain their dividends and share buybacks.

For the oil and gas majors, deficits have been the norm over the past decade. All told, these five companies generated $340 billion in free cash flows from 2010 through the end of 2019, while rewarding their shareholders with $556 billion in share buybacks and dividends—leaving a $216 billion cash shortfall. (See Table 2.) Said differently, over the last decade these five companies covered only 61 percent of their shareholder payouts from free cash flows, while funding 39 percent of those payouts by other means.

Table 2: Five Oil and Gas Supermajors- Free Cash Flow, Shareholder Distributions, Cash Deficits, 2010-2019 (Million $USD)

	Free Cash Flow	Dividends and Buybacks	Surplus (Deficit)	FCF as a Share of Distributions
ExxonMobil	$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%***

Source: IEEFA, based on company financial reports.

Generous dividends and share buybacks have given the global oil majors a superficial appearance of blue-chip financial performance. But closer examination reveals a key weakness in the oil and gas sector's financial fundamentals: Over the past decade, the globe's largest oil and gas companies have been unable to fund payments to shareholders from their core business operations and have instead resorted to other strategies, including borrowing and asset sales, to fund their payments to investors.

Discussion

Executives of the oil and gas supermajors have argued that robust dividends and share repurchases offer a compelling rationale for investing in their companies.[2] Oil executives have managed these shareholder payouts carefully, often aiming to keep dividends stable or growing over time, while using share buybacks as an efficient means to distribute surplus cash.[3]

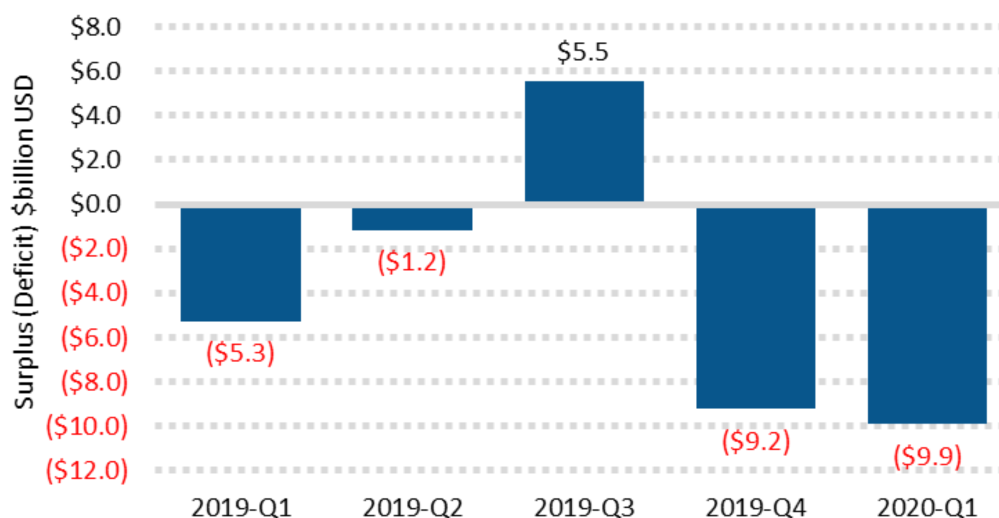
Typically, investors expect private companies to fund payments to shareholders out of free cash flow—the cash generated by the company's operations, minus cash

[2] Energy Intel. Shell CEO: Investors United Only by Appetite for Dividends. October 10, 2019.
[3] Congressional Research Service. Stock Buybacks: Background and Reform Proposals. February 27, 2019.

spent on capital projects.[4] When a company deviates from this standard, investors raise questions about the firm's business model, applying extra scrutiny to its financial underpinnings. Over the past decade, stock market investors have taken an increasingly skeptical view of the oil and gas majors, prompted in part by these companies' sustained inability to produce sufficient free cash flows to fund their dividends and share buybacks. This skepticism has been reflected in poor stock performance, as oil majors' stock prices have decisively trailed the broader stock market over the past decade.

In the aggregate, the five global oil and gas supermajors engaged in deficit spending in four of the last five quarters. (See Figure 1.) Only in the third quarter of last year did these companies collectively report free cash flows that exceeded their payments to shareholders.

Figure 1: Five Supermajors- Free Cash Flow Minus Dividends and Buybacks, Q1 2019-Q1 2020 (Million $USD)



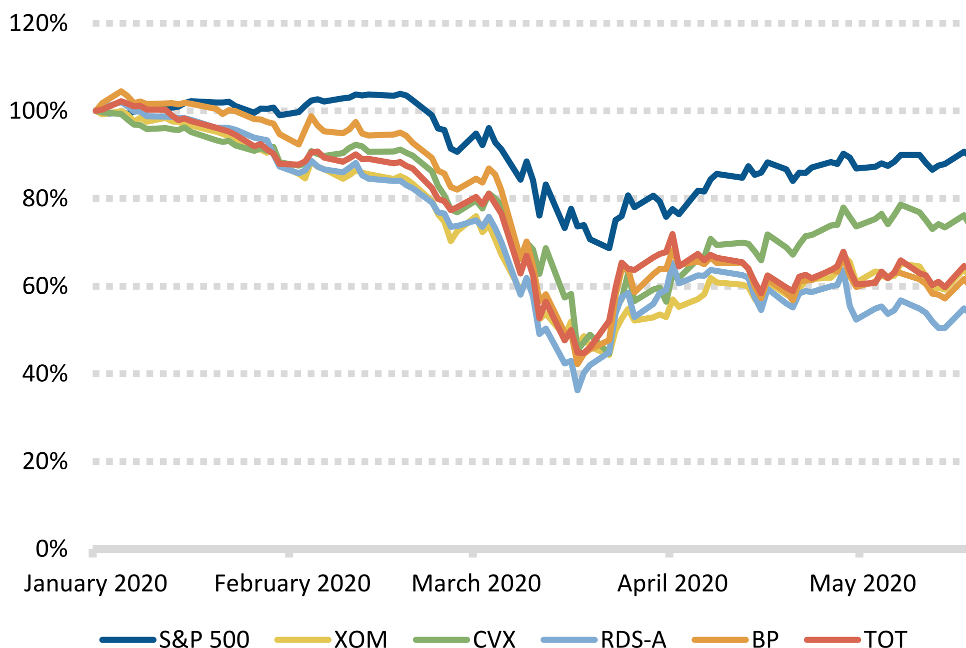
Source: IEEFA, based on company financial reports.

Lackluster free cash flows have prompted the supermajors to borrow money and sell assets to keep cash flowing to investors. Yet investors apparently concluded that these strategies reflect poorly on the firm's long-term financial prospects. Even

[4] Regular warnings are issued by rating agencies, investment publications and the business press about the elevated levels of financial distress that accompany using high levels of debt and asset sales as the means to pay dividends. The warnings are issued as general investment policy and are also specific to the oil and gas industry. See: *The Wall Street Journal*. Big Oil Opts for Payouts Over Debt Rating. February 4, 2016. *Moody's*. Leveraged Finance – US: Tracking The Largest Private Equity Sponsors: LBO Credit Quality Is Weak, Bodes Ill For Next Downturn; *Forbes.* Is Chevron's Debt-Funded 4.5% Yield Really Worth 70x P/E, 300% Payout? March 31, 2016; *The Wall Street Journal*. Borrowing for Dividends Raises Worries. October 6, 2009; *The Money Commando*. Avoid companies that borrow to pay a dividend. September 2016; Stone Fox Capital. Exxon Mobil Dividend Problem. December 16, 2019.

before the twin crises of COVID-19 and the Saudi-Russia price war, stock market valuations already reflected decreasing confidence in the industry. And the industry's stock market performance has only worsened since then, with each of the supermajors stocks decisively trailing the broader stock market since the beginning of the year. (See Figure 2.)

Figure 2: Five Supermajors: Stock Price Trends vs. S&P 500, 2020 YTD



Source: Yahoo Finance.

Today's global oil and gas market—characterized by faltering demand, low prices, and rising volatility—will further weaken the industry's prospects for generating the reliable, robust cash flows that attract investors. In this environment, oil and gas majors now face a troubling choice: They can cut dividends to avoid taking on new debt or they can borrow money to sustain short-term shareholder distributions, while potentially weakening their long-term finances.

The supermajors appear to be responding to this dilemma with divergent strategies. At the end of April, Shell announced that it would cut dividends by two-thirds. The move immediately undercut the company's share price, but may have allowed the company to avoid taking on significant new debt. In contrast, ExxonMobil and Chevron have announced that they will keep dividends steady in the short term. Yet those moves may ultimately backfire. ExxonMobil borrowed heavily to sustain its dividend—the company issued $8.5 billion in new bonds in mid-March, paying a premium to the rates the company paid prior to the coronavirus crisis, and borrowed an additional $9.5 billion less than a month later.[5] Only time will tell

[5] Reuters. Exxon pays more to borrow amid market turmoil. March 17, 2020. Reuters. Exxon raises $9.5 billion to load up on cash while debt market still open to new deals. April 13, 2020.

whether the market will reward these moves. In the meantime, oil and gas investors will have to navigate increasingly treacherous, uncertain, and turbulent waters.

Sources and Methods

For ExxonMobil and Chevron, all data used in this report were drawn from 10-K and 10-Q filings with the U.S. Securities and Exchange Commission (SEC). For Royal Dutch Shell, BP, and Total, all data are taken from 20-F forms filed with the SEC and quarterly financial reports. All spreadsheets and work products for this report are available on request.

Terminology: The five supermajors used slightly different terms and reporting methods in their financial statements. IEEFA believes that variations in definitions, terms, and currencies do not materially impact the basic trends identified in this report. The system of uniform accounting that serves as the basis for formal annual and quarterly company disclosures under U.S. and international securities laws enables reasonable comparisons among the companies on the financial metrics selected for review in this study.

Free Cash Flow: IEEFA calculated free cash flow as net cash from operating activities minus capital expenditures, defined as follows:

- **Net cash from operating activities**. In recent audited financial statements this value was indicated on cash flow statements as "Net cash provided by operating activities" for ExxonMobil, Chevron, and BP, and as "Cash flow from operating activities" for Shell and Total.

- **Capital expenditures.** This value was listed on cash flow statements as "Additions to property, plant, and equipment" for ExxonMobil, "Capital expenditures" for Chevron, "Capital expenditure" for Shell and BP, and "Intangible assets and property, plant and equipment additions" for Total.

Net distributions to shareholders: IEEFA calculated this figure as the sum of dividends and net share buybacks, as defined below:

- **Dividends:** For all companies and in all periods, IEEFA tallied all dividends to common stock shareholders listed on the cash flow statements, excluding all other forms of dividend payments, including dividends to non-controlling interests. ExxonMobil lists such dividends as "Cash dividends to ExxonMobil shareholders." Chevron lists them as "Cash dividends - common stock." Shell lists them as "Cash dividends paid to: Royal Dutch Shell plc shareholders." BP lists them as "Dividends paid - BP shareholders." Total lists them as "Dividends paid: Parent company shareholders."

- **Net share buybacks**: IEEFA combined all common share issuance and buybacks from the cash flow statements into a single net total for each company. For ExxonMobil, we combined "Common stock acquired" and

"Common stock sold." For Chevron, we report "Net sales (purchases) of treasury shares." For Shell, IEEFA reports "Repurchases of shares." For BP, we report the following line items: for 2010, "Net issue of shares" from the 2012 20-F form; for 2011-2016 and 2020Q1, "Net issue (repurchase) of shares"; for 2017-2019, "Repurchase of shares." For Total, we combine all line items labelled "Issuance (repayment) of shares."

- **Shares held in trust**: In its quarterly and annual cash flow statements, Shell lists a separate line item for "Shares held in trust: net sales/(purchases) and dividends received." This figure represents shares and dividends placed in trust on behalf of employees under the company's share-based compensation plans. In each reporting period, IEEFA includes this figure in the company's reported distributions to shareholders. ExxonMobil, Chevron, BP, and Total also provide share-based compensation to employees, but typically repurchase an equal number of shares from the open market, accounting for these transactions as share repurchases.

Exchange rates: Prior to 2011, Total reported its financial results in euros. All figures were converted into U.S. dollars, using the annual exchange rates listed in Total's financial reports.

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

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Clark Williams-Derry, energy finance analyst at IEEFA, served as director of energy finance and research director for the Sightline Institute, a multi-issue sustainability think-tank based in Seattle for 18 years, where his research focused on U.S. and global energy markets. He was also a senior analyst for Environmental Working Group.

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