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Living Beyond Their Means: Cash Flows of Five Oil Majors Can't Cover Dividends, Buybacks

Companies Are Using Stopgap Asset Sales and New Long-Term Debt to Bridge Chronic Shortfalls for Funding Shareholder Dividends

Since 2010, the world's largest oil and gas companies have failed to generate enough cash from their primary business – selling oil, gas, refined products and petrochemicals – to cover the payments they have made to their shareholders. ExxonMobil, BP, Chevron, Total, and Royal Dutch Shell (Shell), the five largest publicly traded oil and gas firms, collectively rewarded stockholders with $536 billion in dividends and share buybacks since 2010, while generating $329 billion in free cash flow over the same period.[1] (See Table 1.)

The companies made up the $207 billion cash shortfall—equal to 39 percent of total shareholder distributions—primarily by selling assets and borrowing money.

Table 1: Five Supermajors: Free Cash Flow, Shareholder Distributions, Cash Deficits, 2010 – 3Q 2019 (Billion $USD)

	Free Cash Flow	Dividends and Buybacks	Deficit
Exxon-Mobil	$137.8	$202.3	($64.5)
BP	$13.2	$62.9	($49.7)
Chevron	$47.3	$90.5	($43.1)
Total SA	$29.4	$56.4	($27.0)
Shell	$101.0	$123.9	($22.9)
Sum, 5 Supermajors	***$328.7***	***$535.9***	***($207.2)***

Source: IEEFA, based on company financial reports. Totals may not add due to rounding.

This practice reflects an underlying weakness in the fundamentals of contemporary oil and gas business models: revenues from the supermajors' operations are not covering their core operational expenses and capital expenditures. This helps explain why energy has been the poorest-performing sector in the stock market in recent years despite oil prices having more than doubled since hitting $29 per barrel in 2016. Generous dividends and share buybacks give companies the appearance of reliable blue-chip financial performance when, in this case, the opposite is true. A closer look at how the oil and gas majors are actually funding

[1] See Appendix for methodology.

their dividends reveals that each quarter the companies seem like increasingly speculative investments.

Discussion

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

Investors typically[4] expect private companies to fund these types of shareholder payouts with free cash flow (FCF)—the cash generated by the company's operations, minus cash spent on capital projects.[5] Significant departure from this standard requires enhanced diligence.

Since 2010, the oil majors in our sample have, in aggregate, generated sufficient cash to cover their operating expenses and capital expenditures (capex); that is, each of the supermajors generated positive FCF over the decade. But not one of the world's five largest private sector oil companies was able to cover its payments to shareholders through FCF alone.[6]

The oil majors' cash shortfalls varied by year. (See Figure 1.) In 2013 and 2014, high oil prices helped the companies generate ample cash flows, but the companies sustained even higher levels of capital spending and shareholder distributions, leading to steep cash deficits. And in 2015 and 2016, a crash in oil prices

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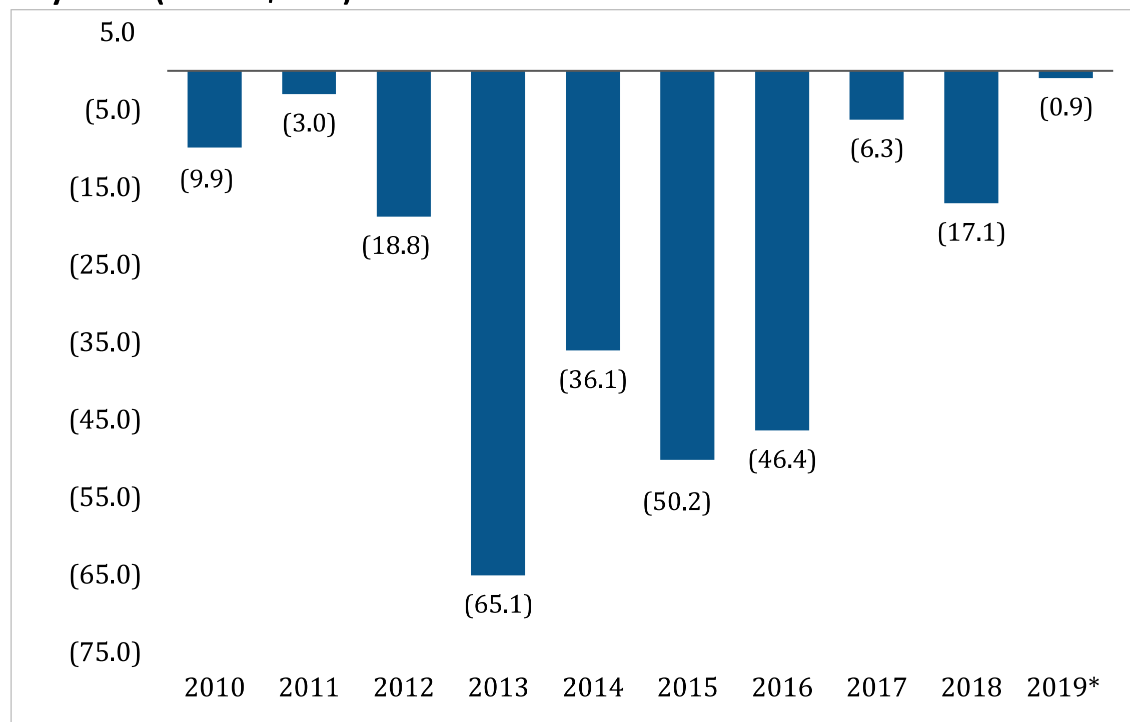
[2] Energy Intel. Shell CEO on Dividends. October 10, 2019.
[3] CRS.gov. Stock buybacks: Background and reform proposals. February 27, 2019.
[4] Regular warnings are issued by rating agencies, investment publications and the business press about the elevated levels of financial distress that accompany 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.
[5] Stone Fox Capital. Exxon Mobil Dividend Problem. December 16, 2019.
[6] In the late 1980's Exxon 's management led an effort to change the financial metrics used to assess the company's performance. Rather than being assessed on the basis of quarterly cash and dividend payments, Exxon argued that its longer-term investment metric was the most effective measure of its performance. The campaign was largely successful, and most of the industry adopted Exxon's measure known as *Return on Capital Employed* (R.O.C.E.). See: Steve Coll, Private Empire, ExxonMobil and American Power, New York, Penguin Books, 2012, pps. 47-51. With the collapse in oil prices in 2014 and substantial value loss for investors, the era of assessing oil and gas companies based on this long-term measure is being rejected and greater weight is being accorded to the more typical measures used to judge company performance across sectors. The Wall Street Journal, Investors to Big Oil: Make it Rain. November 1, 2019

constrained revenues, leading to two consecutive years of negative free cash flows--and two more years of cash deficits.

Figure 1. Five Supermajors: Free Cash Flow Minus Dividends and Buybacks (Billion $USD)



Source: IEEFA, based on company financial reports. Totals may not add due to rounding.
**2019 numbers through the end of the third quarter.*

The five oil supermajors employed a range of strategies to deal with their cash shortfalls. BP and Total, for example, trimmed dividends after oil prices fell in 2015 and 2016, helping the companies narrow their cash deficits.

Asset sales have been a crucial source of funding of dividends and share buybacks for the supermajors. Shell, for example, sold $68 billion in assets from 2010 through the third quarter of 2019, including asset sales of $11 billion in 2017 and $6 billion in 2018 that helped the company bolster cash reserves even as it boosted shareholder payouts.

More asset sales are likely over the coming years, as each of the oil majors[7] has announced that portions of their global reserves are for sale.These moves are part of a broader industry-wide trend of raising cash by selling off poorly positioned or underperforming assets.

[7] Rystad.com. Majors' global selling spree could fetch $27 billion. November 18, 2019.

Further, all five of the supermajors borrowed significant funds over the decade, taking on a cumulative $122 billion in additional long-term debt as part of the company's annual cash strategy needed to keep cash payments to shareholders flowing out the door. (See Table 2.)

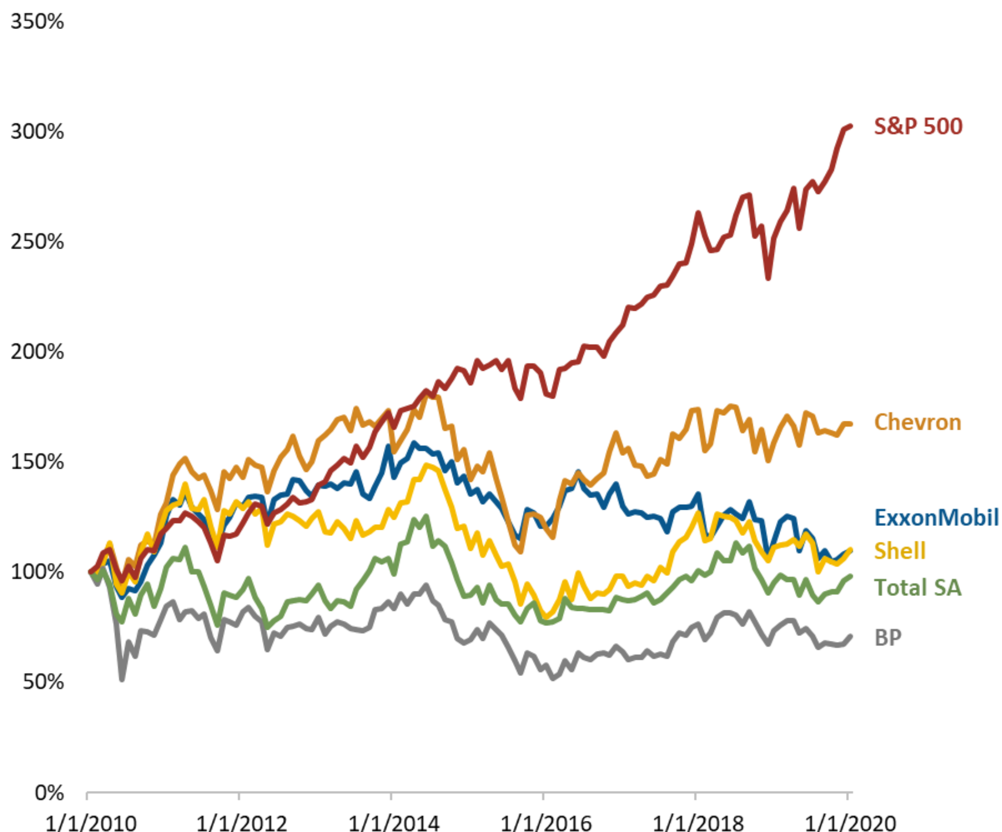
Table 2: Five Supermajors: New Long-term Debt 2010 – 3Q 2019 (Billion $USD)

	New Long-term Debt
Exxon-Mobil	$17.9
BP	$33.3
Chevron	$15.1
Total SA	$19.5
Shell	$36.2
Sum, 5 Supermajors	***$122.0***

Source: IEEFA, based on company financial reports. Totals may not add due to rounding.

In recent years, investors have reacted to the supermajors' financial management with skepticism. Oil prices have more than doubled since their 2016 lows, allowing the supermajors to boost dividends and share buybacks. Yet their stock prices have lagged behind the broader stock market. (See Figure 2.)

Figure 2. Stock Prices of the Five Supermajors vs. the S&P 500 (January 2010 = 100%)



Source: Yahoo Finance

Moving forward, the oil and gas supermajors are struggling to define their business models and attract new investors. Stock markets reflect decreasing investor confidence in the industry. So, the supermajors have emphasized their ability to generate cash through dividends and share buybacks, as a key measure of their financial value. But that strategy also requires greater caution: as demonstrated in this report, 61 percent of the payments to shareholders over the past decade were covered by cash flows from their core business activities.

Clearly, the supermajors' attempts to attract investors by rewarding shareholders with short-term cash have failed to protect the industry's share prices. The energy sector has been a weak performer in the S&P 500 for a decade, and the supermajors' lackluster results have contributed to that underperformance.

Appendix: Data and Methodology

Summary data, 2010-2019Q3 (Billion $USD)

	Free Cash Flow	Dividends and Buybacks	Deficit	Asset Sales	New Long-term Debt
Exxon-Mobil	$137.8	$202.3	($64.5)	$43.3	$17.9
BP	$13.2	$62.9	($49.7)	$70.0	$33.3
Chevron	$47.3	$90.5	($43.1)	$35.0	$15.1
Total SA	$29.4	$56.4	($27.0)	$30.4	$19.5
Shell	$101.0	$123.9	($22.9)	$68.1	$36.2
Sum, 5 Supermajors	***$328.8***	***$536.0***	***($207.2)***	***$246.7***	***$122.0***

Source: IEEFA, based on company financial reports. Totals may not add due to rounding.

All data used in this report were drawn from filings with the U.S. Securities and Exchange Commission (SEC). Annual data for 2010 through 2018 was drawn from 10-K forms for ExxonMobil and Chevron, and from 20-F forms for Shell, BP, and Total. For 2019, data was drawn from quarterly reports through the third quarter of the year.

IEEFA took additional steps to check the validity of the trends that are suggested by the data. In a few instances, the authors checked with company investor relations to determine the accuracy of the formal securities disclosures. IEEFA also reviewed numerous credit opinions and analytical updates conducted by Moody's on each of the companies for the period covered in this paper. Moody's analytical systems treat many of the data sets used in this report differently. IEEFA did not change any number based on these studies and relied exclusively on the corporate data reported in each company's financial filings. The Moody's reports were used as sensitivity checks on trends and as additional explanation to support IEEFA's data gathering, analysis and conclusions.

All spreadsheets and work products for this report are available on request as are any of the independent studies used for sensitivity checks.

Terminology: The 5 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 strength of 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 additions to long-term debt: Total long term-debt was listed as "Long-term debt" for ExxonMobil, Chevron, and Shell, as "Finance debt" for BP, and as "Non-current financial debt" for Total. Where possible, IEEFA excluded lease obligations from long-term debt. Lease obligations were listed in different ways over time for each company. ExxonMobil reported "capitalized lease obligations" as a separate line item on its balance sheet. Chevron reported "capital lease obligations" as part of its long-term debt for 2017 and 2018, but as a separate line item in prior years. Shell listed "finance lease liabilities" in notes to the balance sheet. BP did the same for "net obligations under finance leases," and Total for "financial lease obligations."

Asset Sales: In recent financial statements, ExxonMobil listed asset sales as a single line item: "Proceeds associated with sales of subsidiaries, property, plant and equipment, and sales and returns of investments." Chevron reported asset sales as "Proceeds and deposits related to asset sales and returns of investment." Shell's cash flow statements had separate listings for "Proceeds from sale of property, plant and equipment and businesses" and "Proceeds from sale of joint ventures and associates," which IEEFA summed to a single total for asset sales. BP listed "Proceeds from disposals of fixed assets" separately from "Proceeds from disposals of businesses, net of cash disposed," which IEEFA summed to a single total. For Total, IEEFA calculated asset sales as the sum of "Proceeds from disposals of intangible assets and property, plant and equipment" and "Proceeds from disposals of subsidiaries, net of cash sold."

Dividends: For all companies and in all periods, IEEFA tallied all dividends to shareholders of common stock listed on the cash flow statements, excluding all other forms of dividend payments, including dividends to non-controlling interests.

Net share buybacks: The 5 companies reported buybacks of common shares in varied ways. Some listed a single number for net purchases/sales; others with separate line items for issuances and repurchases. And some companies listed separate totals for issuance repurchases of common shares and treasury shares. We combined all share issuance and buybacks into a single net total for each company, in each year.

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

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 conducts research and analyses on financial and economic issues related to energy and the environment. The Institute's mission is to accelerate the transition to a diverse, sustainable and profitable energy economy. www.ieefa.org

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