The Oil Industry Has Been in Financial Trouble for Years

Federal Support for the Oil Industry Might Help Investors but Won’t Save Jobs

Virtually every industry faces severe financial challenges in the wake of the coronavirus pandemic, and the oil and gas industry is no exception. But if you listen to oil company spokespeople, you might believe that their financial struggles began in March, only after the global pandemic had sent the economy reeling and oil demand plummeting.

Yet in reality, the US oil industry was in crisis even before the coronavirus crisis began. The so-called “fracking boom,” now responsible for most of America’s oil and gas production, has long been a financial bust. Fracking is expensive, and fracked wells deplete quickly—a double-whammy that has created financial stresses for the country’s oil and gas sector for more than a decade.

Now that US oil companies are pressuring Washington for coronavirus support, it’s vital to remember that the industry’s financial struggles began long before COVID-19. Any bailout for the oil industry would mostly reward investors for risky bets that had gone bad well before the coronavirus crisis started.

Collapsing Stock Prices and Bankruptcies: Symptoms of a Failing Industry

The S&P 500—a stock portfolio of large US companies—has risen by 57 percent since 2014. But oil and gas stocks have lagged far behind. One widely traded portfolio of oil and gas producers fell by an astonishing 84 percent since 2014. (See Figure 1.)

Even big oil and gas companies, such as ExxonMobil and Chevron, have trailed the broader stock market for years. And the overall energy sector, once a clear leader in US stock markets, has been the worst performer in the S&P 500 over the past decade.

Poor stock market performance is the clearest sign that Wall Street views the oil and gas sector as a financial underperformer with weak profits, massive debts, and cloudy prospects.
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Many oil and gas companies have borrowed heavily, and many have been unable to service their debts. Since 2015, North America’s oil and gas producers have suffered at least 215 corporate bankruptcies, in the process restructuring more than $129 billion in debt. Much of this debt—loaned by investors, pension funds, and banks—was written off in bankruptcy and will never be repaid.

Oil and Gas Companies Pay More to Shareholders Than They Earn from Sales

Over the past decade the oil and gas supermajors—corporate giants such as ExxonMobil, Chevron, and Royal Dutch Shell—have paid out far more cash to investors than they’ve generated by selling oil, gas, and refined products like gasoline and diesel. (See Figure 2.)

These companies have covered their cash shortfalls by borrowing money and selling off pieces of their companies—moves that gave short-term infusions of cash, but saddled the companies with debt and undermined their long-term profitability.

Despite the Production Boom, Jobs in Oil Extraction Have Declined

Fracking allows oil companies to produce more oil with less labor. Oil and gas extraction in the US employed fewer workers in March of this year than before the fracking boom got into full swing—and also fewer than in the late-1970s. (See Figure 3.)

Oil sector employment will stay low until prices rise high enough to justify the expense of drilling. If oil companies boost production now, they will simply deepen the supply glut that is keeping prices low and undermining the industry’s financial health.
Government Financial Support May Help Investors but Won’t Solve Oil & Gas Industry’s Problems

Over the short term, direct government financial support for the oil and gas industry might protect banks and investors from some losses on bad loans. But it won’t change the long-term structural forces that have led the U.S. oil industry to burn through cash and shed workers.

At this stage, there are other measures that would help stabilize the oil industry’s finances. For example, direct regulation of oil and gas production volumes could help restore financial balance to the industry by preventing wasteful overproduction and by alleviating the supply gluts that have driven U.S. oil prices to historic lows. Similarly, to provide employment to workers and communities affected by the economic downturn, oil companies can be incentivized to clean up their growing stockpiles of inactive oil and gas wells.

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