

Wall Street calls for better returns; shale gets thrifty



Bloomberg/New York

Investors urged shale drillers to spend less and boost returns. They seem to be listening.

Producers from Anadarko Petroleum Corp to Occidental Petroleum Corp are trimming capital budgets after a slip in oil prices in the fourth quarter. Marathon Oil Corp is pledging more than \$750mn of cash flow over the next two years – even if crude stays at \$50 a barrel. And Chevron Corp is ramping up its share buyback programme to \$4bn this year.

“Every other company is now actively resisting increased spending, and actively promoting their cash return metrics,” Paul Sankey, an analyst at Mizuho Securities USA LLC, said in a note to clients on Thursday.

That effort may already be showing early signs of success. Fourth-quarter earnings from energy companies in the S&P 500 reported in the past couple of weeks have so far come in at 18% higher than analysts’ estimates on average, according to data compiled by Bloomberg. That’s more than double the average seen in any other sector.

Much of the US oil and gas sector has yet to report, but the companies that have – including Exxon Mobil Corp and Chevron – suggest an industry focused perhaps more than ever on cash flow over production growth after several years of poor performance.

“We’re seeing the early signs of capital discipline returning to the industry,” Evercore ISI analyst James West said.

Despite the collapse of oil prices in the fourth quarter, Big Oil was a standout success. All five of the world’s largest publicly traded oil companies beat analyst expectations, with Royal Dutch Shell Plc leading the pack with a cash flow figure

triple what it was a year earlier. Though production slipped, the focus is now growing cash flow, Shell chief financial officer Jessica Uhl said.

Maybe, oil majors have the shale revolution to thank for that shift, according to Chevron chief executive officer Mike Wirth. Cheap oil from US shale basins meant producers needed to streamline – or they'd fall behind. Shale "has forced us to get smarter about how we do everything else," Wirth said in an interview.

Among the independent drillers, almost everyone is cutting projected capital spending, bowing to Wall Street pressure as companies seek to show investors they can live within their means. Fail to do so, and their stock price will feel the pain. Pioneer Natural Resources Co saw its shares dip more than 5% on concerns its spending cut wasn't big enough to guarantee it wouldn't outspend cash flow.

Still, it may take more than a handful of spending cuts to assuage years of investor frustration with the industry. The S&P 500 Energy Index is up 13% this year, less than the 20% rise in oil prices. It's doing better than the broader S&P 500, though, which is up 9.5% for the year.

The companies that actually drill and pump for those producers haven't been left behind in the broader energy rally. Halliburton Co and Schlumberger Ltd, the world's biggest oilfield service companies, are riding strong international growth that's softening the impact of a weakening US market.

Schlumberger, which was one of the worst performing stocks in the entire S&P 500 last year, won plaudits for its capital austerity while keeping its dividend intact.

The rig count has also exceeded expectations in the first quarter so far, with overall activity looking like it's on pace to surprise on the upside in the first half, according to Wells Fargo analysts Jud Bailey and Coleman Sullivan. But with drilling budgets down in 2019, question marks remain over the second half of the year.