



# How Does UK Oil & Gas Attract Capital?

## A View From The World's Largest Asset Manager

**Mark Hume**  
**Portfolio Manager**  
**BlackRock Natural Resources**

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# Capital Competition

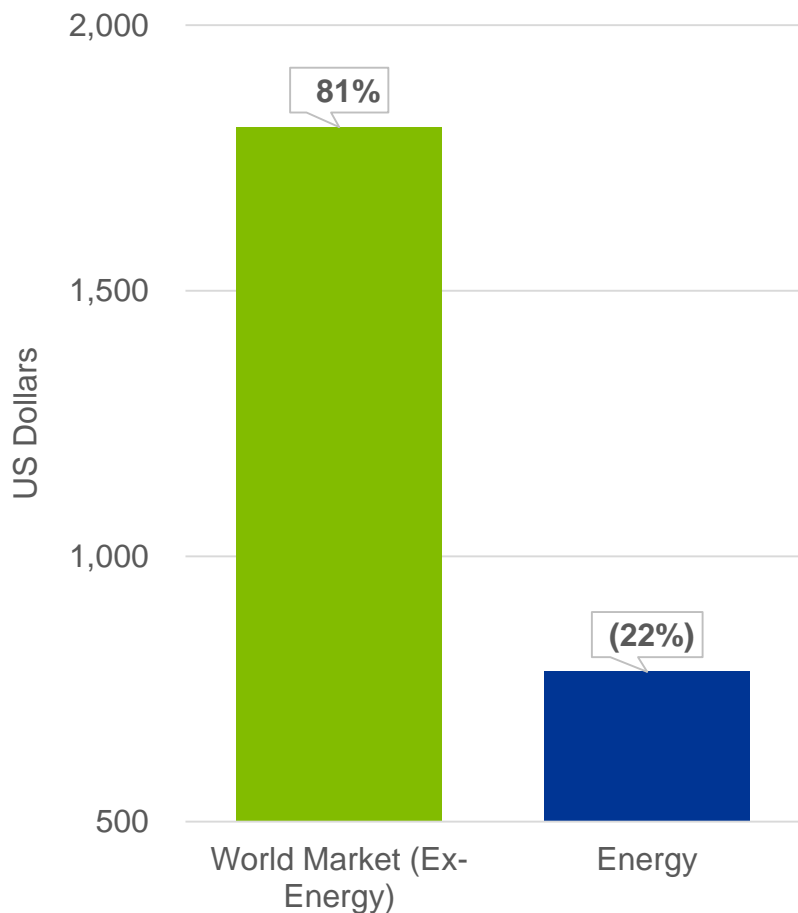
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“Capital will always go where it’s needed and stay where it’s well treated”

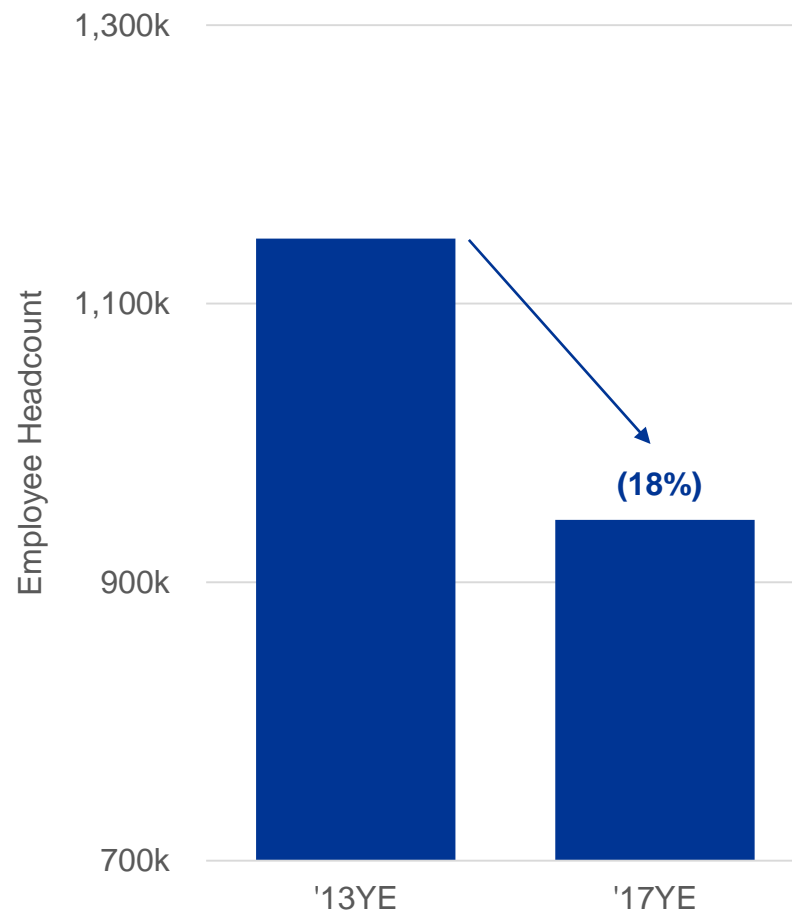
- *Walter Wriston*

# The Energy Industry Has To Compete With All Sectors

Value of Initial US\$1,000 Investment from 2008\*



Industry Headcount Reduction 2017 versus 2013\*\*



Source: Bloomberg. \*MSCI All Country World Indices (ACWI). USD returns assuming dividends are reinvested from 21 May 2008 through 25 November 2018. \*\*Industry Headcount sample set of 47 publicly-listed global oil and gas companies.

# The 3-Ds of Oil & Gas

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## The 3-Ds of Oil & Gas

### Debt

- Low leverage 1.0x-1.5x Net Debt:Cash Flow
- Funding sources - 'live' within cash flow

### Discipline

- Low Cost of Supply (CoS);
- Focus on returns not growth;
- Management/employee incentives

### Distribution

- Capital allocation – if reinvestment RoR < Weighted Average Cost of Capital (WACC) return cash to shareholders

Source: BlackRock, 2018. For illustrative purposes only.

## Where Are We In The Cycle?

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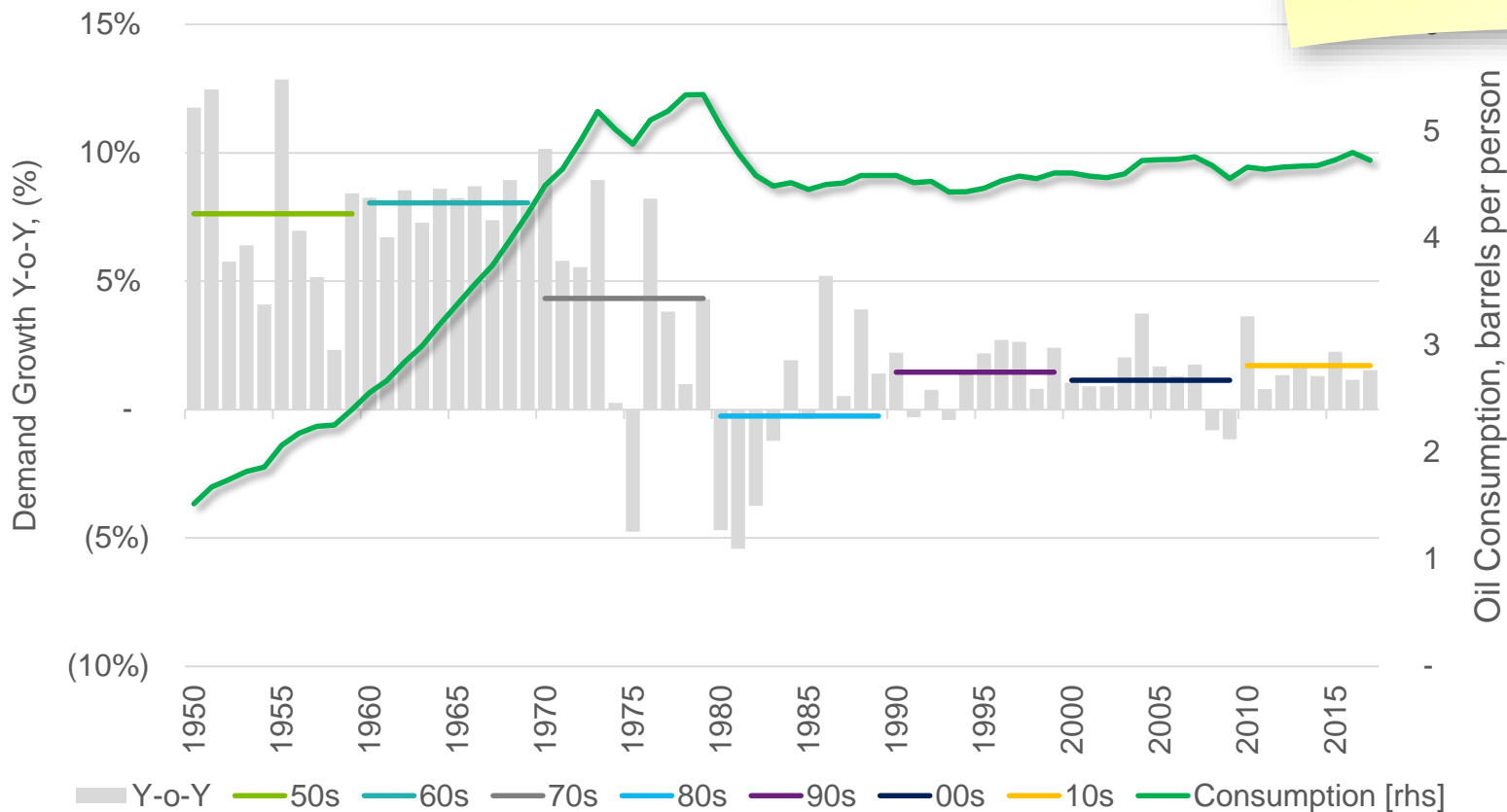
“History doesn't always repeat itself. Sometimes it just screams, "Why don't you listen to me?" and lets fly with a big stick.”

*- John W. Campbell, Jr.*

# Where Are We In The Cycle – Framing The Current Cycle

*Demand has been incredibly healthy this cycle – it is supply which is causing much of the volatility in oil markets*

Global Oil Demand Growth and Per Capita Consumption, 1950-2017

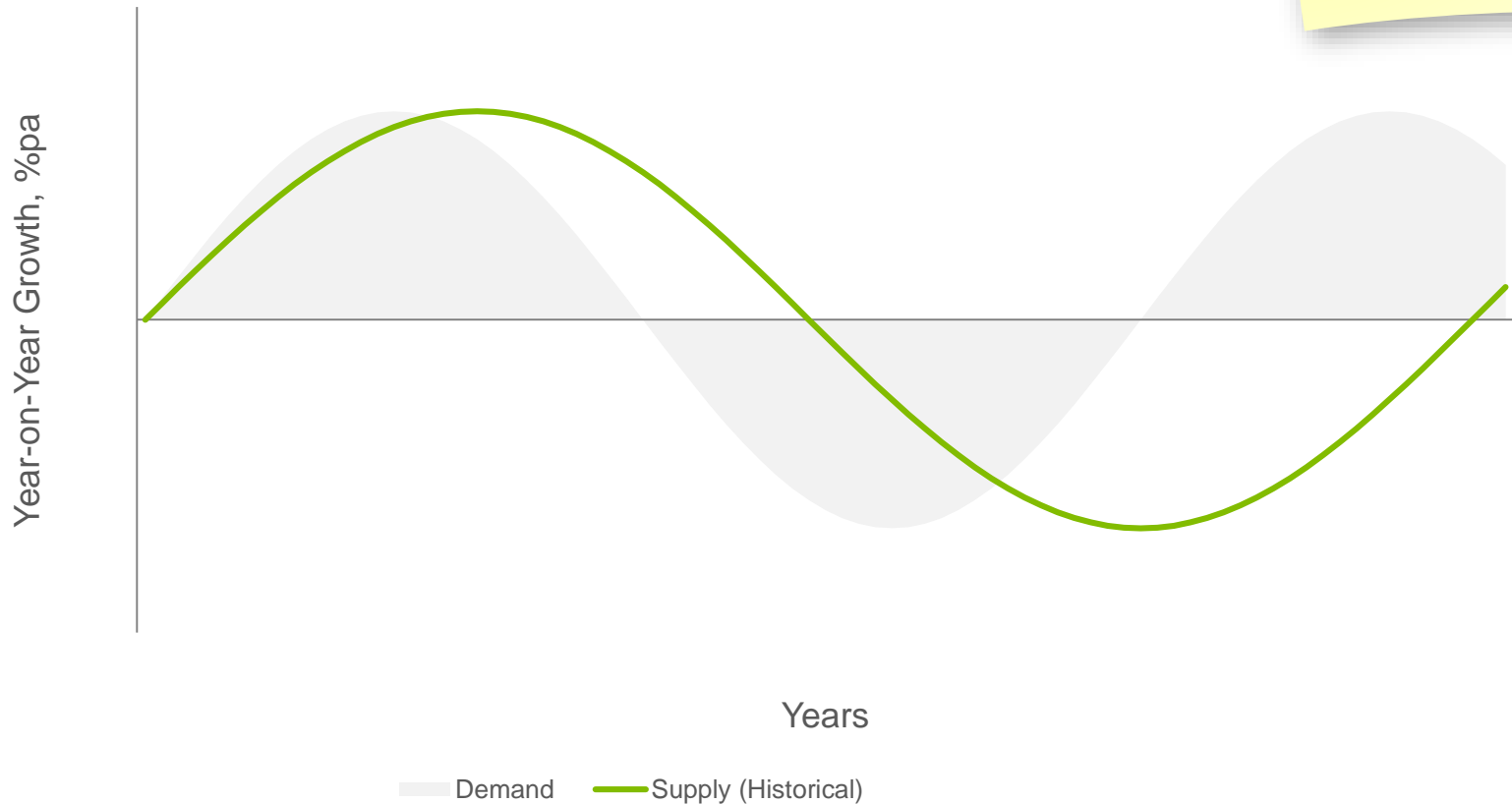


Sources: BP Statistical Review of World Energy 2018, Bloomberg, EIA, IEA, UN Population Division.

# Where Are We In The Cycle – Supply

Global oil markets are cyclical due to a mismatch between supply and demand. Historically, supply has been much slower to respond to changes in price than demand.

Global Oil Supply / Demand Growth, %pa



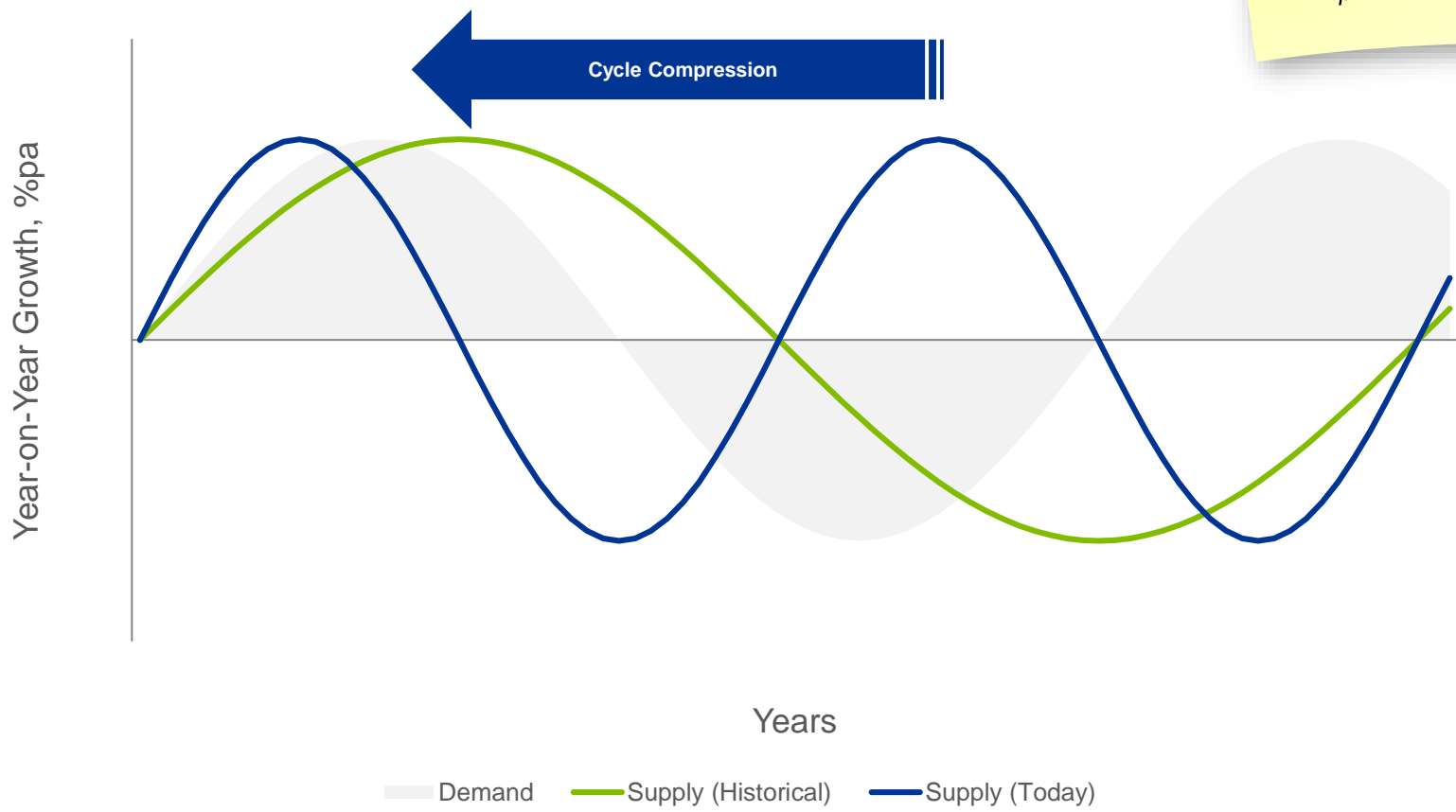
Source: BlackRock estimates over a 4 year period. There is no guarantee that any forecasts made will come to pass. For illustrative purposes only.



# Where Are We In The Cycle – Supply

Shale and OPEC 'time-to-market' is much faster than conventional oil – leading to faster 'reaction' times to changes in price. Shale has a tendency to 'overreact' in both directions leading to price volatility.

Global Oil Supply / Demand Growth, %pa

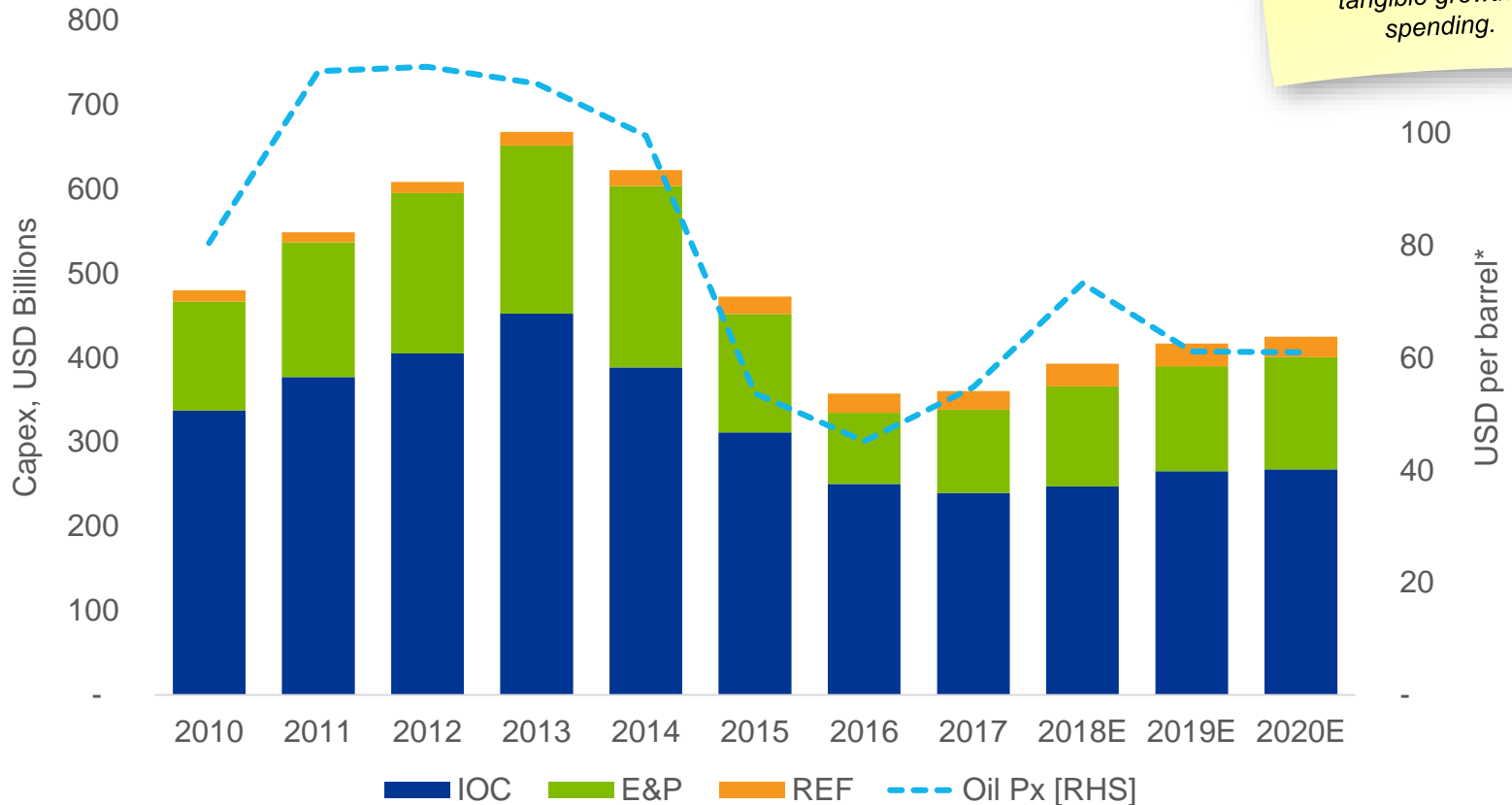


Source: BlackRock estimates over a 4 year period. There is no guarantee that any forecasts made will come to pass. For illustrative purposes only.

# Where Are We In The Cycle – Capital Discipline

*The industry is focused on returns over growth. This means a protracted period of capital restraint – at least from the larger companies. North America (shale) remains the only area for tangible growth in spending.*

## Upstream Capital Investment Outlook

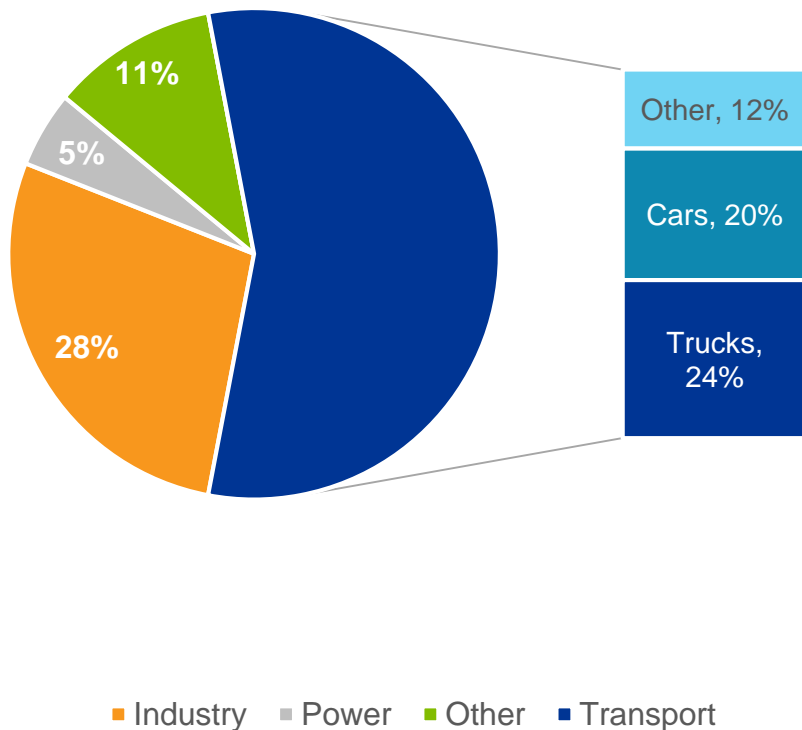


Sources: Bloomberg, as of November 2018. IOC: Integrated Oil Company; E&P:= Exploration & Production; REF:= Refining & Marketing. Capital expenditure estimates from 110 publicly-listed energy companies. \*Brent front-month historical and futures pricing. There is no guarantee that any forecasts made will come to pass.

# Where Are We In The Cycle – Threat Of Substitution

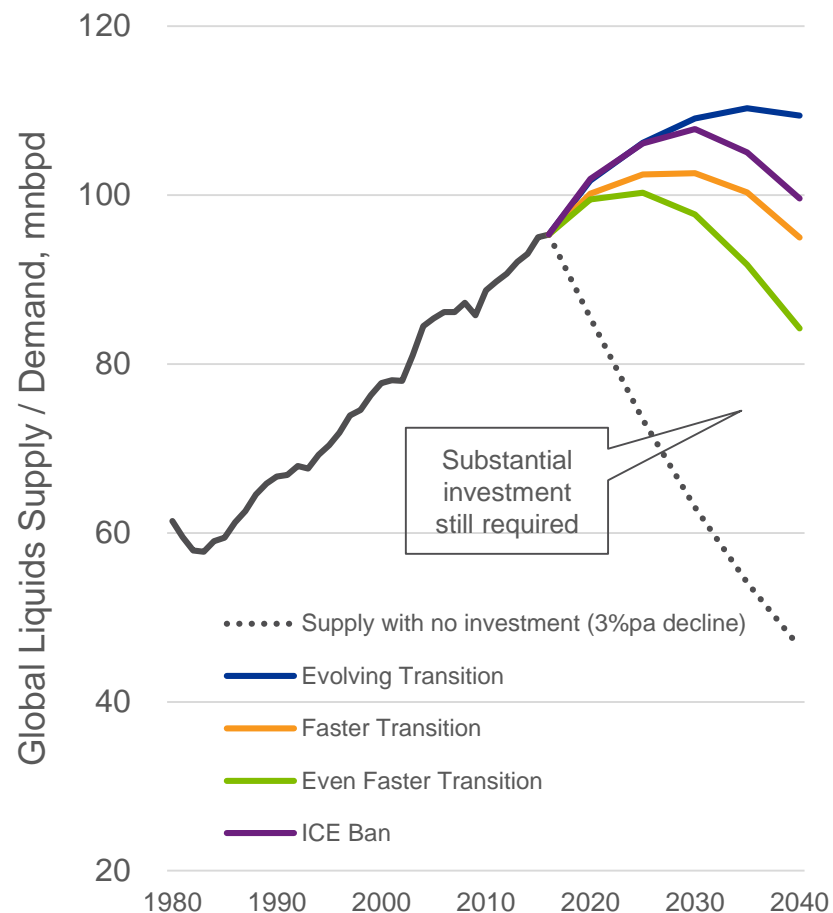
## Global Oil Consumption by End-User

Global Oil Demand in 2015  
(95mnbpd)



Source: BP Energy Outlook, 2016. For illustrative purposes only.

## Investment In Future Supply Is Still Required

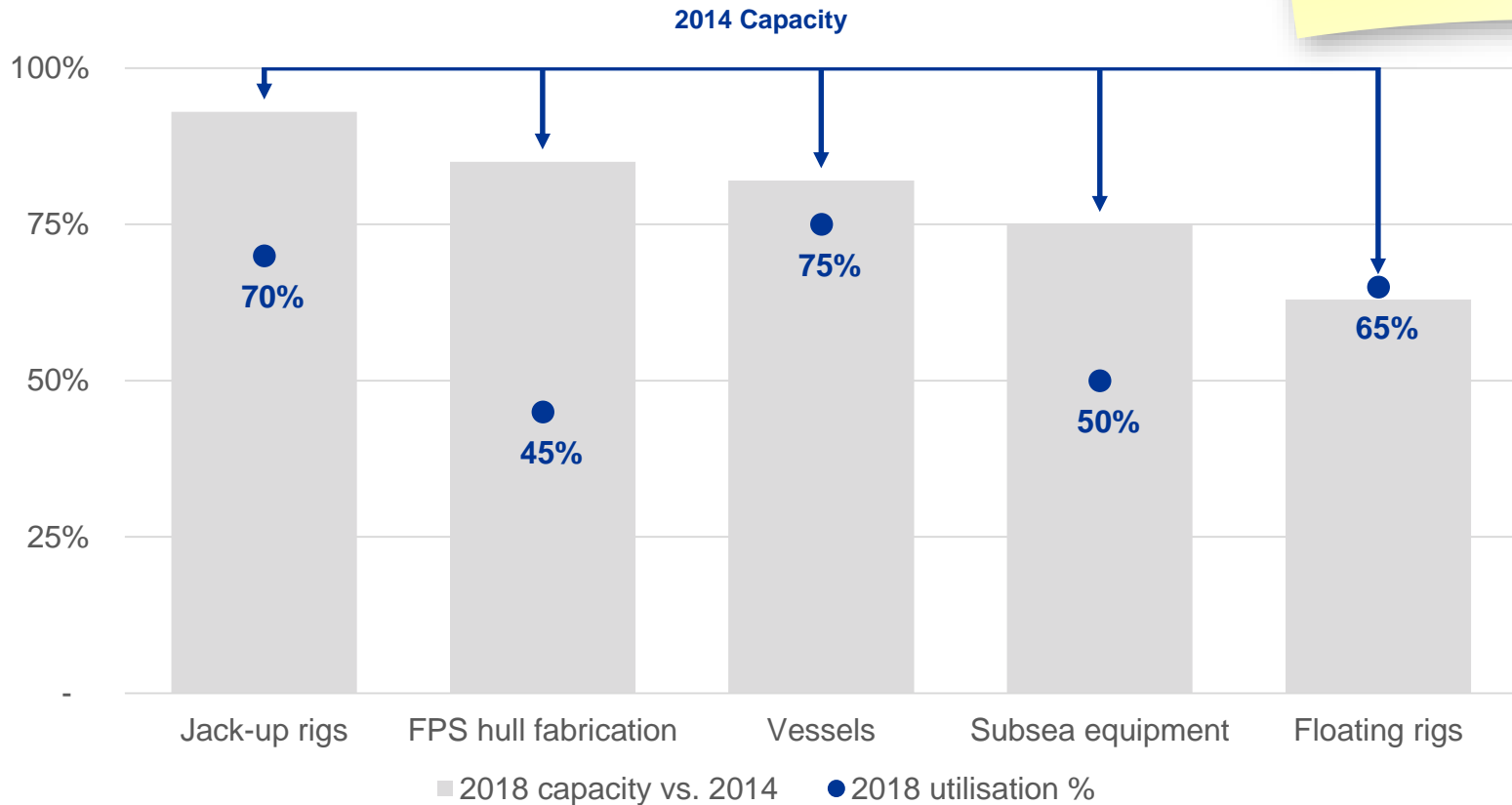


Source: BP Energy Outlook, 2018. **There is no guarantee that any forecasts made will come to pass.**

# Where Are We In The Cycle – Suppliers

*Despite substantial capacity reduction, many parts of the oilfield service sector remain at low levels of utilization – leaving much of the pricing power with customers*

## Current Supply Chain Capacity and Utilisation



Source: Wood Mackenzie, September 2018.

# Competitive Landscape

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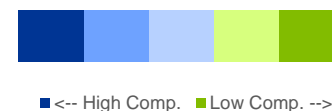
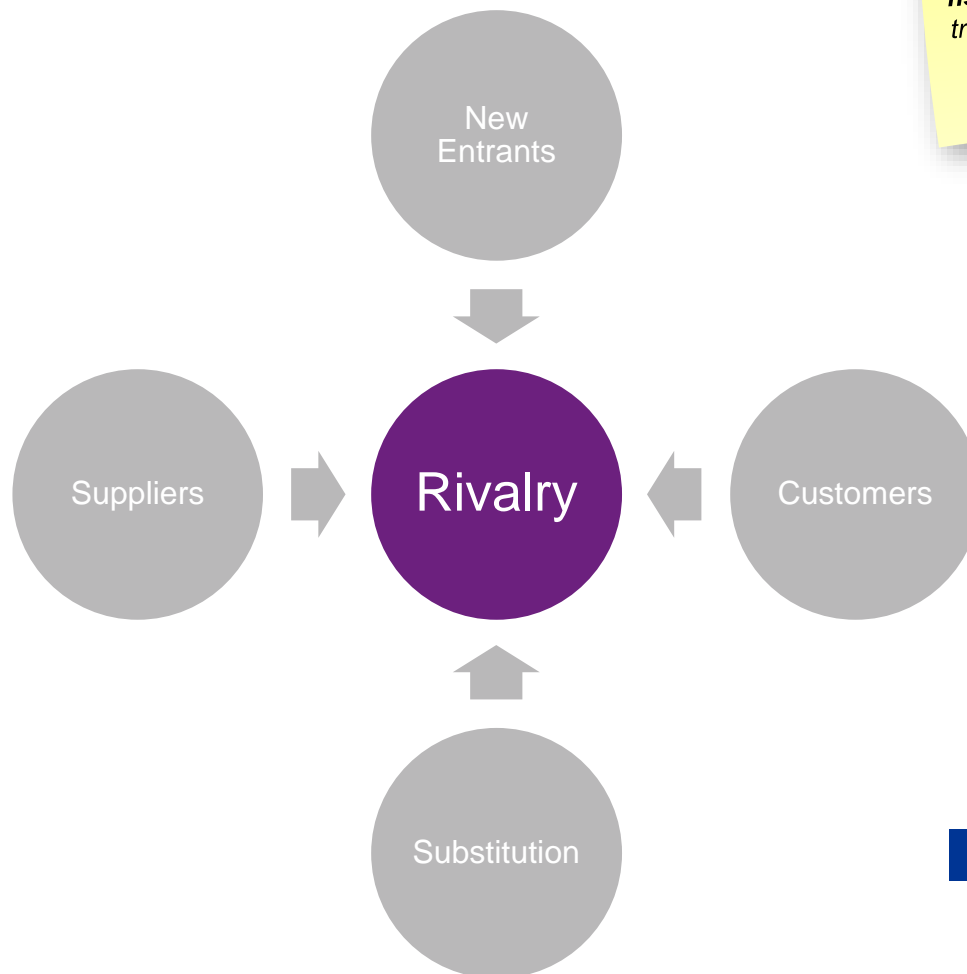
“The supply of cheap oil has plateaued”

- *D. King, Director Smith School of Enterprise, University of Oxford (2005)*

# Competitive Forces

Overall Competition Has Evolved But Remains High

**Other Risk Factors –**  
**Mature basin** with diminishing organic growth potential (**decline**), ageing infrastructure (**safety**), **fiscal instability** (UK govt. track-record has been pro-cyclical), **abandonment costs**



Source: BlackRock, 2018. For illustrative purposes only. The numbers reflect our interpretation of the degree of competition in each category, with 1 reflecting the highest competition and 5 reflecting the lowest.

## Return On Capital

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“You can fool some of the people all of the time, and all of the people some of the time, but you can not fool all of the people all of the time.”

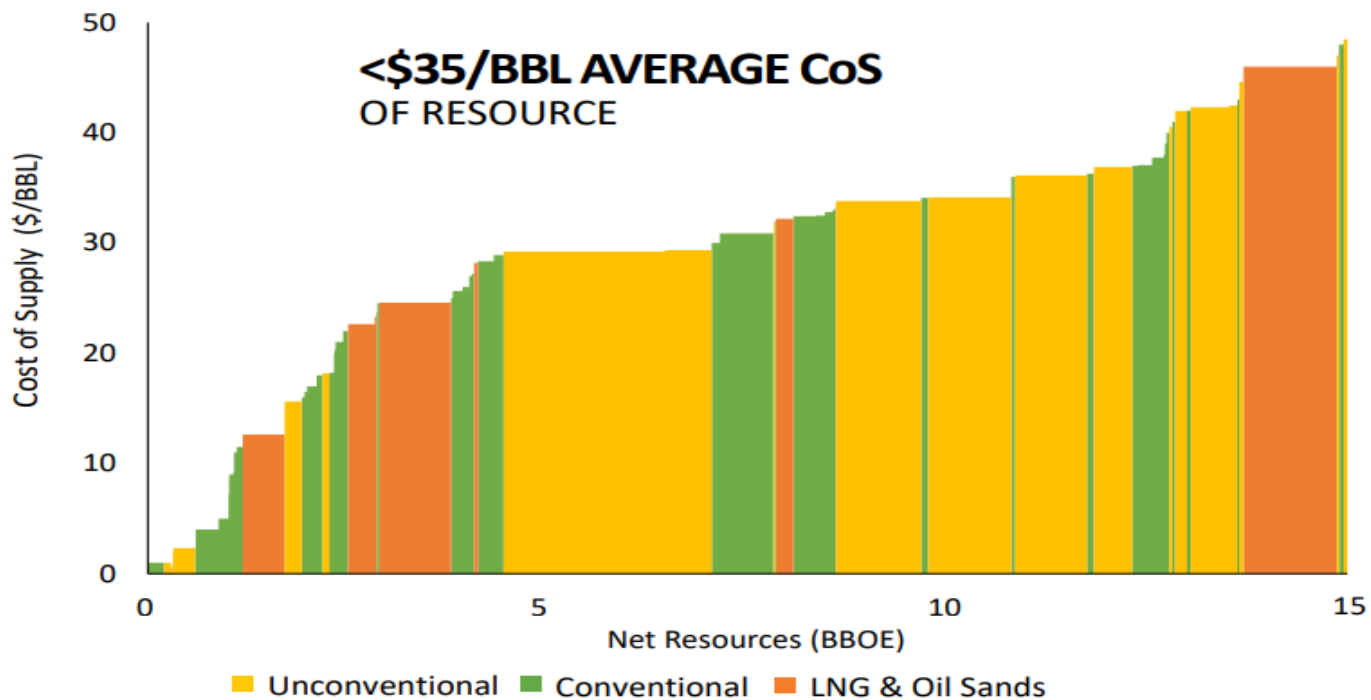
*- Abraham Lincoln*

# Return On Capital – High Quality Inventory

## Low Cost of Supply (CoS)

Having a clear understanding of capital allocation choices within your portfolio – will yield better, more timely decisions

**<\$50/BBL Cost of Supply Resource**



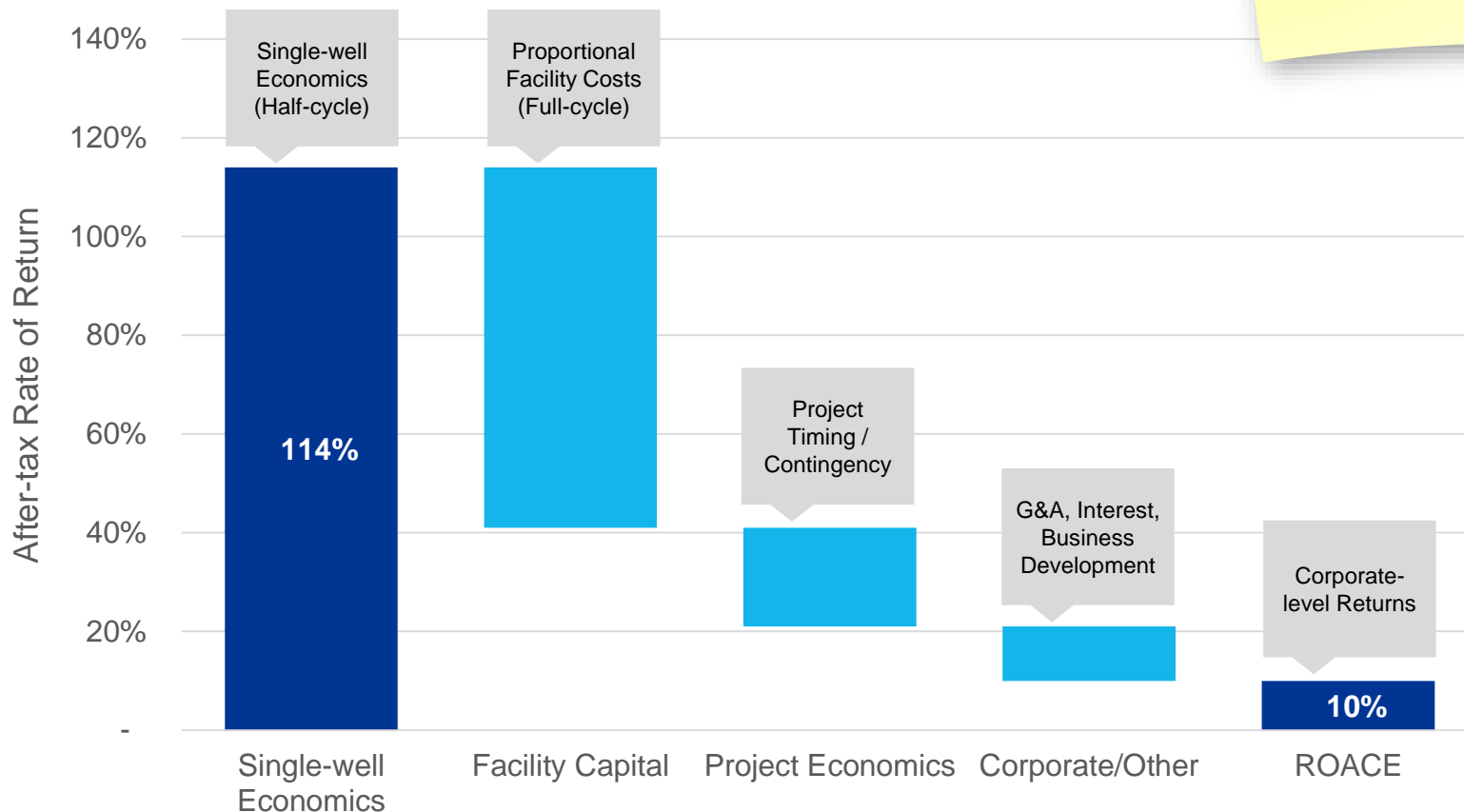
Source: ConocoPhillips corporate presentation, November 2017. Figures shown in USD. For illustrative purposes only.



# Return On Capital – Don't Be Fooled

*Only by delivering real returns at the corporate level, can you build a sustainable and profitable business for the long-term*

## Full Cycle And Corporate Returns



Source: Arc Resources corporate presentation, January 2017 and BlackRock estimates. There is no guarantee that any forecasts made will come to pass. G&A refers to the General & Administrative expenses of a company. For illustrative purposes only. The chart reflects returns over the full life of the project (~20 years).

## Conclusion

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## Conclusion – Debt, Discipline and Distribution

**Survive @ \$40/bbl;**

**Thrive @ \$50/bbl;**

**Don't Compromise @ \$60/bbl**

### Investment Framework



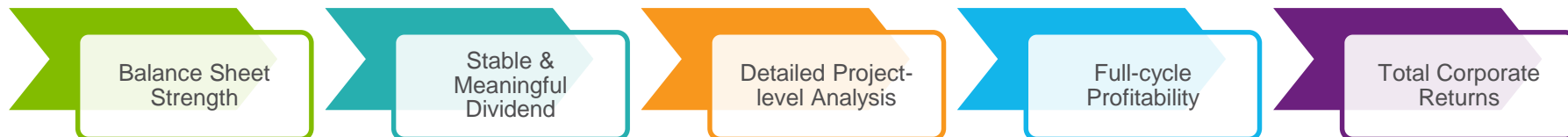
Source: BlackRock, 2018. For illustrative purposes only. Figures shown in USD.

# Appendix

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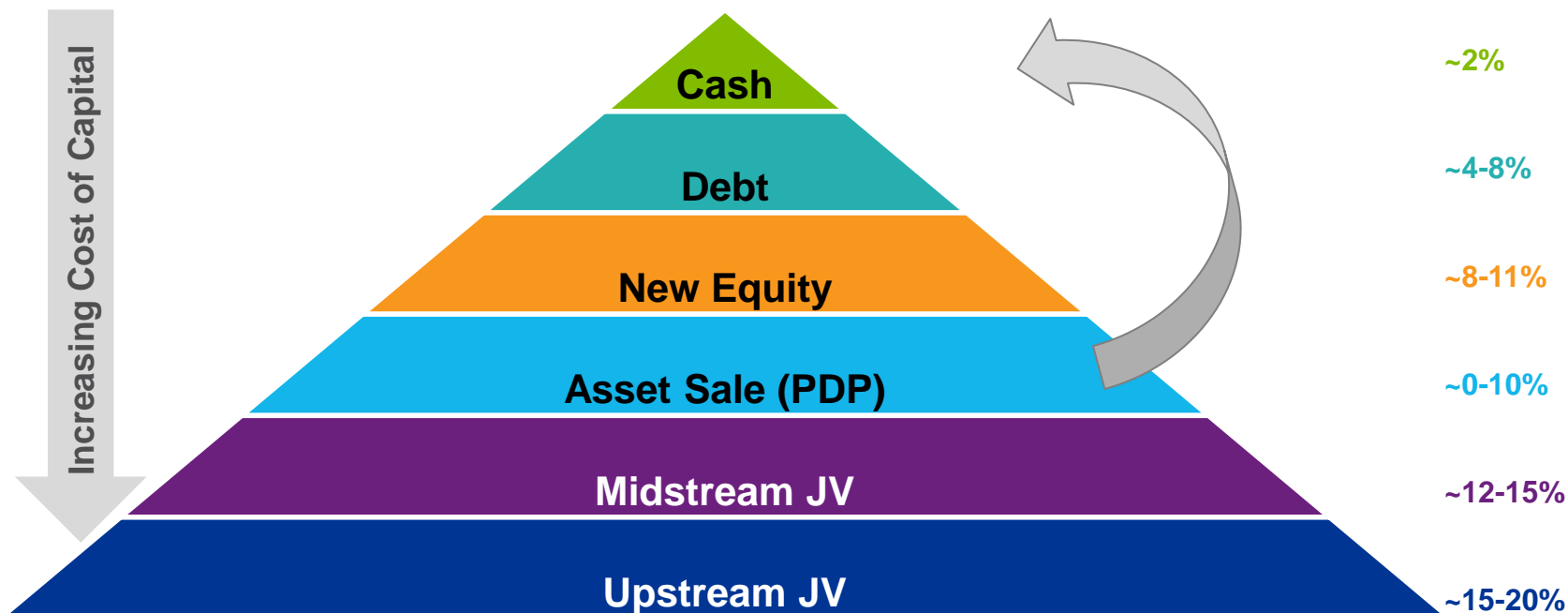
# Capital Allocation Principles

## Financial Discipline



## Funding Sources

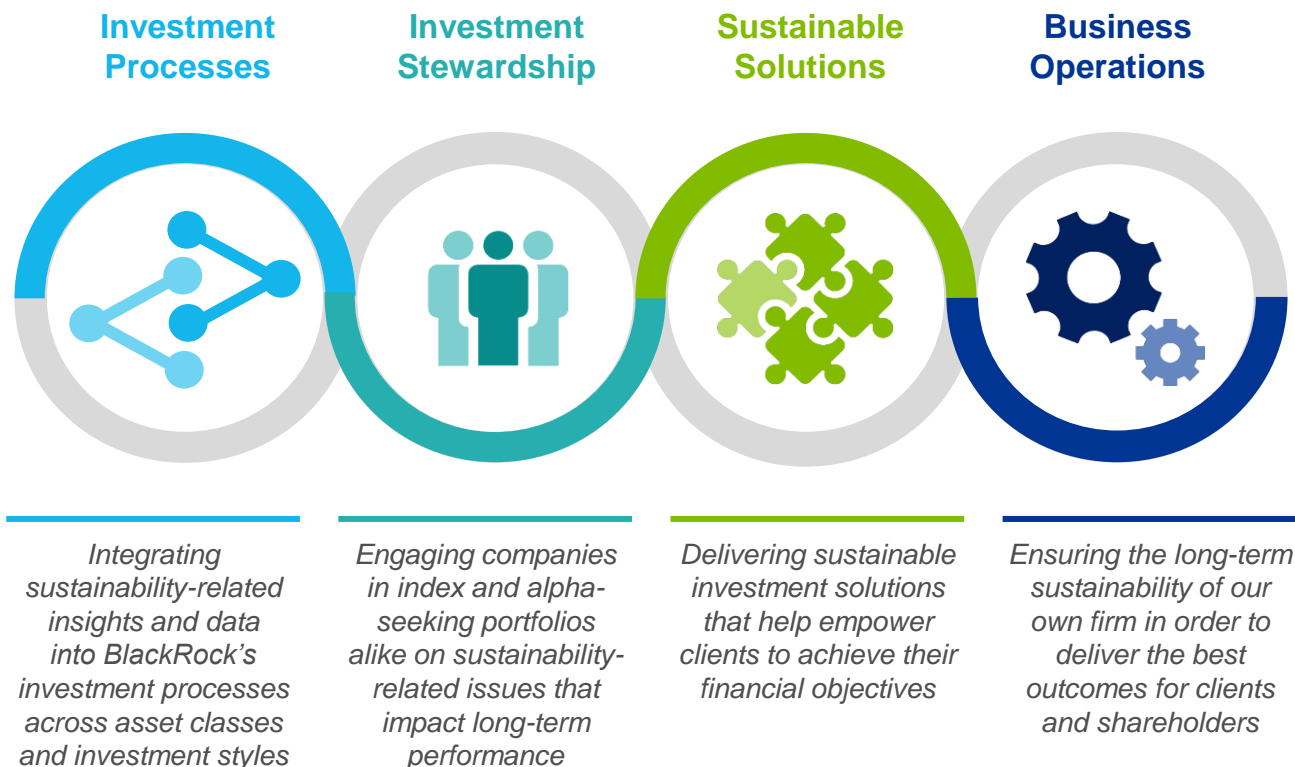
## Cost of Capital\*



Source: Arc Resources corporate presentation, November 2018. \*BlackRock estimates of indicative cost of capital. For illustrative purposes only.

# BlackRock's Mission Statement On Sustainability

BlackRock believes environmental, social and governance issues have real financial impacts over the long term. As we work to create better financial futures for clients, we strive to be a leader in the way we incorporate sustainability into our:



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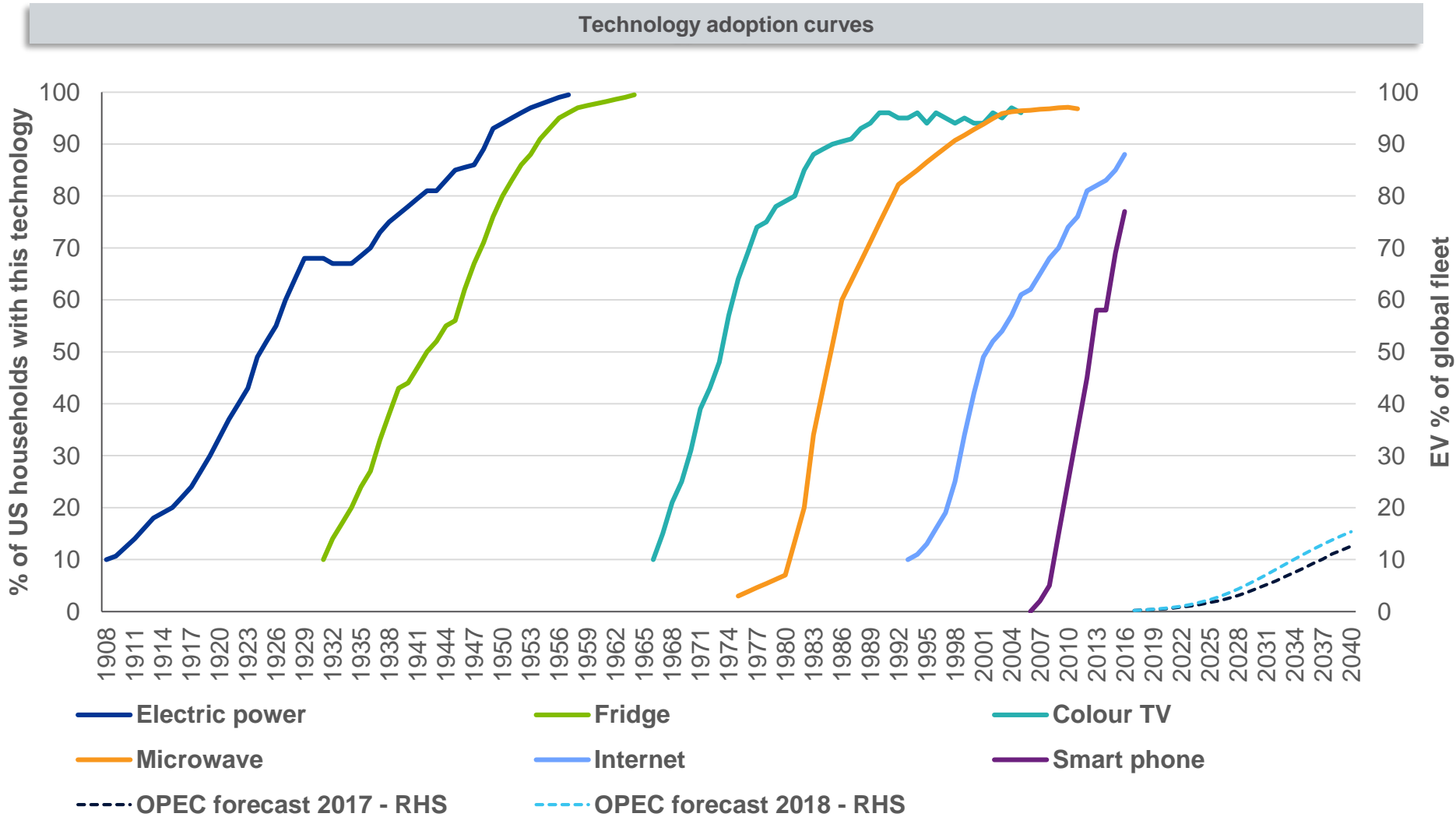
“ To **prosper** over time, every company must not only deliver financial performance, but also show how it makes a **positive contribution to society.**”

– Larry Fink, 2018 Letter to CEOs

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Source: BlackRock, October 2018. For illustrative purposes only.

# The Pace Of Energy Transition Continues To Be Under-estimated...



Source: BlackRock and OPEC, October 2018. For illustrative purposes only. There is no guarantee that any forecasts made will come to pass.

## Risks

**Capital at risk.** The value of investments and the income from them can fall as well as rise and are not guaranteed. The investor may not get back the amount originally invested.

Past performance is not a reliable indicator of current or future results and should not be the sole factor of consideration when selecting a product or strategy.

Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Fluctuation may be particularly marked in the case of a higher volatility fund and the value of an investment may fall suddenly and substantially. Levels and basis of taxation may change from time to time.



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