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Energy Finance

Financial News for Major Energy Companies, Fourth Quarter 2006

Overview

The "Financial News for Major Energy Companies" is issued quarterly to report recent trends in the financial performance of the major energy companies. These include the respondents to Form EIA-28 (Financial Reporting System (FRS)), with the exception of the FRS companies that do not issue quarterly earnings releases or do not provide separate information for the company's U.S. operations. Nineteen major energy companies[1] reported overall net income (excluding unusual items) of $23.0 billion on revenues of $258.9 billion during the fourth quarter of 2006 (Q406). The level of net income for Q406 was 18 percent lower than in the fourth quarter of 2005 (Q405) (Table 1). Net income for Q406 decreased primarily as a result of much lower natural gas prices, reduced foreign production of natural gas, and lower U.S. refining margins.

Overall net income (excluding unusual items) for all of 2006 reached $104.8 billion on revenues of $1.1 trillion. The level of net income for 2006 was 16 percent higher than for 2005 (Table 1). Net income increased on the strength of increases in foreign crude oil production, worldwide natural gas production, foreign refinery throughput, worldwide crude oil prices, and U.S. refinery margins.

Overall, the petroleum line of business (which includes both oil and natural gas production and petroleum refining/marketing) registered a 28-percent decrease in net income between Q405 and Q406. A 30-percent decrease in oil and gas production net income augmented a 22-percent decrease in refining/marketing net income. All lines of business reported lower earnings in Q406 relative to Q405 with the exception of worldwide chemical operations. (Note: corporate net income and the total net income of the lines of business differ because (1) some items in corporate net income are nontraceable, such as interest expense, and are not allocated to lines of business, and (2) the number of companies reporting line-of-business net income varies.)

For all of 2006 the petroleum line of business generated an 8-percent decrease in net income relative to 2005. A 16-percent increase in refining/marketing net income combined with a 4-percent increase in oil and gas production net income. Most of the lines of business reported higher earnings in 2006 relative to 2005; domestic oil and gas production was the exception.

Energy Price News

The crude oil price for Q406 increased by almost three percent relative to a year earlier and the price of natural gas fell more than two-fifths. The U.S. refiner average acquisition cost of imported crude oil increased from $52.01 per barrel in Q405 to $53.39 per barrel in Q406 (Table 2). (See the current and recent issues of the *Short-Term Energy Outlook* for explanation of these price changes and those discussed below.) This was the eighteenth consecutive quarter in which crude oil prices increased relative to their year-earlier levels, after six consecutive quarters of falling or unchanged crude oil prices (relative to a year earlier).

The average U.S. natural gas wellhead price decreased 41 percent between Q405 and Q406, falling from $10.17 per thousand cubic feet to $6.03 (Table 2). This is the second consecutive quarter in which domestic natural gas prices fell relative to the year-earlier quarter and comes on the heels of a streak of nine consecutive quarters in which natural gas prices increased or were unchanged relative to their year-earlier levels.

The crude oil price over all of 2006 was 21-percent higher than for 2005, increasing from $48.96 per barrel to $59.02. Alternatively, 2006's average price of natural gas was 14 percent lower than the average for 2005, falling from $7.45 per thousand cubic feet to $6.41 (Table 2).

Worldwide Petroleum Earnings

Earnings from worldwide oil and natural gas production operations (i.e., upstream operations) decreased 30 percent between Q405 and Q406. Slightly lower foreign earnings were accompanied by a much larger (in terms of both nominal and percentage changes) decrease in domestic earnings.

Table 1. Corporate Revenue and Net Income[a], Net Income by Lines of Business and Functional Petroleum Segments, and Operating Information for Major Energy Companies

(Number of companies reporting given in parentheses)

	Q405	Q406	Percent Change[b]	2005	2006	Percent Change
	Financial Data					
	(Millions of Dollars)		(%)	(Millions of Dollars)		(%)
Corporate						
Revenue (17)[c]	297,568	258,929	-13.0	1,067,182	1,109,551	4.0
Net Income (17)	27,968	22,990	-17.8	90,310	104,779	16.0
Worldwide Lines of Business Net Income						
Petroleum (19)	33,450	24,182	-27.7	114,286	122,023	6.8
Oil and Gas Production (15)	25,213	17,763	-29.6	84,514	87,513	3.5
Refining/Marketing (11)	8,237	6,419	-22.1	29,771	34,509	15.9
Gas and Power (7)	778	643	-17.3	3,314	3,415	3.1
Chemicals (7)	1,407	1,900	35.0	6,657	7,777	16.8
Domestic Net Income						
Oil and Gas Production (10)	9,571	5,725	-40.2	32,448	30,382	-6.4
Refining/Marketing (11)	6,294	4,412	-29.9	21,951	26,522	20.8
Foreign Net Income						
Oil and Gas Production (5)	8,971	8,875	-1.1	30,936	37,802	22.2
Refining/Marketing (5)	2,198	2,007	-8.7	7,820	7,987	2.1
	Operating Data					
Oil Production	(Thousands of Barrels/Day)		(%)	(Thousands of Barrels/Day)		(%)
Domestic (14)	3,011	3,143	4.4	3,293	3,113	-5.5
Foreign (10)	5,024	5,249	4.5	4,845	5,080	4.8
Natural Gas Production	(Million Cubic Feet/Day)		(%)	(Million Cubic Feet/Day)		(%)
Domestic (15)	17,010	18,082	6.3	18,134	17,995	-0.8
Foreign (10)	17,673	17,056	-3.5	16,719	16,810	0.5
Refinery Throughput	(Thousands of Barrels/Day)		(%)	(Thousands of Barrels/Day)		(%)
Domestic (11)	11,700	12,194	4.2	12,142	12,176	0.3
Foreign (5)	6,269	6,262	-0.1	6,070	6,268	3.3

[a] Net income excludes unusual items. Because consolidated net income includes corporate nontraceables and eliminations, it is not equal to the sum of the lines of business net income.

[b] Percent changes are calculated from unrounded data.

[c] The number of companies reporting net income from petroleum operations is greater than the number reporting corporate revenue and corporate net income because the U.S. operations of BP and Royal Dutch/Shell are included in the results of the U.S. lines of business, but not in the foreign or corporate results because the companies are foreign based.

Note: Both the worldwide oil and natural gas production and refining/marketing lines of business include companies that reported domestic and foreign operations separately and those that do not separate domestic and foreign results. Thus, the number of companies with worldwide oil and natural gas production operations is greater than the sum of the companies reporting domestic results and those reporting foreign results. The same is also true for refining/marketing operations.

Sources: Compiled from companies' quarterly reports to stockholders.

Table 2. U.S. Energy Prices and the U.S. Gross Refining Margin

	Q405	Q406	Percent Change	2005	2006	Percent Change
U.S. Energy Prices[a]						
Refiner Acquisition Cost of Imported Crude Oil ($/barrel)	52.01	53.39	2.6	48.96	59.02	20.5
Natural Gas Wellhead Price ($/thousand cubic feet)	10.17	6.03	-40.7	7.45	6.41	-13.9
U.S. Gross Refining Margin ($/barrel)[b]	19.54	15.28	-21.8	18.32	19.30	5.3

[a] Energy Information Administration, *Short-Term Energy Outlook* , (Washington, DC, December 12, 2006 and March 6, 2007), Table 4.
[b] Compiled from data in Energy Information Administration, *Petroleum Marketing Monthly* , DOE/EIA-380 (Washington, DC), Table 1, Table 4 and Table 5; and Energy Information Administration, *Monthly Energy Review* , DOE/EIA-0035, (Washington, DC) Table 3.2b.
Note: The U.S. Gross Refining Margin is the difference between the composite wholesale product price and the composite refiner acquisition cost of crude oil.

Overall earnings for domestic upstream operations in Q406 were 40 percent lower than in Q405 (Table 1). Domestic upstream earnings decreased relative to a year ago as the 41-percent decline in domestic natural gas prices (Table 2) overwhelmed the effects of slightly higher crude oil prices, and higher crude oil and natural gas production (Table 1). The results were consistent as all ten companies that reported separate net income for domestic upstream operations recorded lower earnings than a year ago. Various company press releases note several factors that collectively resulted in lower earnings. The factors include field shutdowns and divestitures, which lead to reduced production levels; higher operating and exploration costs; and substantially lower U.S. natural gas prices.

Domestic upstream operations were 6 percent lower in 2006 than in 2005 (Table 1). Domestic upstream earnings decreased relative to a year ago as the upward pressure on earnings generated by a large increase in crude oil prices was overwhelmed by a similar reduction in domestic natural gas prices (Table 2), and by reduced crude oil and natural gas production (Table 1).

Net income from foreign upstream operations in Q406 decreased 1 percent relative to Q405 (Table 1), as three of the five companies that reported separate net income from foreign upstream operations reported a decrease in Q406 relative to Q405. A 5-percent increase in foreign crude oil production put upward pressure on earnings, while a 4-percent decline in foreign natural gas production put downward pressure on earnings from this line of business. Company press releases noted that earnings fell as lower natural gas prices received by the companies, higher operating costs, and decreased production (due to renegotiated production-sharing contracts and natural field declines). The companies reporting higher earnings from a year ago cited much higher crude oil prices received and increased production.

Earnings from foreign upstream operations for all of 2006 were 22 percent higher than over all of 2005 (Table 1), as all five companies that reported separate net income from foreign upstream operations reported an increase in Q406 relative to Q405. Foreign earnings primarily increased on the strength of higher crude oil prices (Table 2). A 5-percent increase in foreign crude oil production put upward pressure on earnings, while a scant increase in foreign natural gas production put additional upward pressure on earnings from this line of business. Company press releases noted that earnings rose due to higher crude oil prices and increased production (due to increasing production from existing fields and asset acquisitions).

Earnings from worldwide refining and marketing operations (i.e., downstream operations) decreased 22 percent between Q405 and Q406 as lower worldwide industry margins offset higher U.S. refinery throughput. Lower foreign earnings accompanied much lower domestic earnings, resulting in a large decrease from $8.2 billion in Q405 to $6.4 billion in Q406. Earnings over all of 2006 were 16-percent higher than for 2005 as slightly higher foreign earnings were augmented by much larger domestic earnings, which were underpinned by slightly higher industry wide refining margins (Table 2).

Profits from domestic downstream operations decreased 30 percent in Q406 relative to Q405 as a decrease in gross margins was somewhat offset by a 4-percent increase in refinery throughput. Petroleum product stocks were 4 percent higher than in Q405, putting downward pressure on gross refining margins (the per-barrel composite wholesale product price less the composite refiner acquisition cost of crude oil), which decreased by 22 percent between Q405 and Q406 (Table 2) Increased domestic refinery throughput relative to Q405 by those U.S. majors reporting domestic refinery throughput (Table 1), which was attributed to recovery from the effects of Hurricanes Katrina and Rita, put upward pressure on earnings. The net effect of these and other factors was that U.S. refining/marketing earnings decreased almost $2 billion, to $4.4 billion in Q406 (Table 1). The performance of the eleven companies that reported U.S. refining/marketing earnings was consistent as nine reported lower earnings (and the balance reported higher earnings). Lower refining and marketing margins, lower earnings from trading, operational problems, and higher operating costs were noted in press releases by some of the companies reporting lower earnings. Higher earnings were associated with companies that made large acquisitions and reported higher regional refining margins.

Earnings from domestic downstream operations increased 21 percent in 2006 relative to 2005 as upward pressure on earnings from a 5-percent increase in industry-wide gross margins was slightly magnified by a less-than-1-percent increase in refinery throughput, but somewhat offset by petroleum product stocks that were consistently higher over 2006 than 2005. The results were mixed as seven of the eleven companies reporting earnings for domestic refining/marketing operations reported higher earnings and the balance reported lower earnings. Among the reasons given for higher earnings were higher refining and marketing margins, and higher refinery throughput. Alternatively, lower earnings were attributed to lower refining margins, higher operating costs, and reduced refinery throughput.

Earnings from foreign downstream operations decreased 9 percent between Q405 and Q406 (Table 1). Refinery throughput was unchanged between Q405 and Q406 (Table 1), but lower industry-wide margins (Figure 1) in both Europe (by $3.17/barrel) and Asia/Pacific (by $3.08/barrel) put downward pressure on earnings. The company results were consistent for those companies separately reporting foreign downstream earnings as four of the five reported lower earnings. The companies reporting lower earnings noted lower refining margins, and lower throughput and product sales due to divestitures. Alternatively, higher earnings were largely attributed to foreign currency effects.

Profits from foreign downstream operations increased 2 percent between 2005 and 2006 (Table 1). Industry-wide effects were mixed as refining margins were consistently lower in 2006 than in 2005 in both Europe and Asia/Pacific, which put downward pressure on earnings, while daily average refinery throughput was higher (Table 2), putting upward pressure on earnings. Similarly, the results were mixed as three companies reported higher earnings and two companies reported lower earnings.

Worldwide Downstream Natural Gas and Power

Worldwide downstream natural gas and power earnings decreased 17 percent (Table 1) due to a variety of factors. Five of the seven companies reported lower earnings than a year earlier, but for a variety of reasons. Lower earnings were attributed to such varied factors as lower NGL prices, asset divestitures, and warmer weather, which resulted in reduced retail natural gas and electricity sales. Higher earnings were attributed to increased revenue from electricity generation.

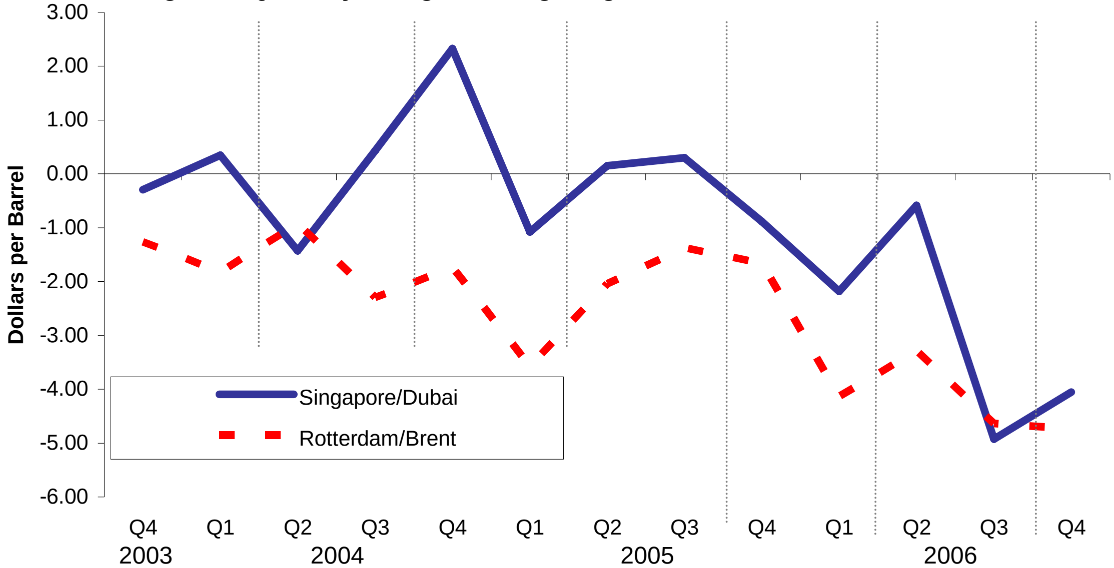
Profits from worldwide downstream natural gas and power operations increased 3 percent between 2005 and 2006 (Table 1). The results were mixed as three companies reported higher earnings (noting gains from hedging activity and greater retail natural gas and electricity sales) and four companies reported lower earnings (due to asset divestitures and outages due to planned maintenance).

Worldwide Chemical Operations

Higher margins fuel a 35-percent increase in earnings from the majors' chemical operations. Four of the seven companies reporting results for this line of business recorded higher earnings, resulting in more than a one-third increase in earnings from the majors' chemical operations in Q406 relative to Q405 (Table 1). The higher earnings were chiefly due to Exxon Mobil (which accounted for 65 percent of Q406 chemical net income and 80 percent of the increase in earnings relative to Q405). The foremost reason for higher earnings was higher margins (due to much lower natural gas prices) and increased sales volumes. Further, some companies noted reduced operating costs. Alternatively, lower earnings were attributed to lower margins and lower sales volumes.

Profits from worldwide chemical operations increased 17 percent between 2005 and 2006 (Table 1). Five companies reported higher earnings and two companies reported lower earnings. Higher earnings were due to higher margins and sales volumes, and lower operating costs. Lower earnings may be attributed to BP's exit from worldwide chemical operations along with diminished product demand and operating difficulties, which were noted in press releases.

Figure 1. Quarterly Foreign Refining Margins, 2003 - 2006



[a] Gross refining margin is defined as netback crude oil price less spot crude oil price. The netback price is calculated by multiplying the spot price of each refined product by the percentage share in the yield of a barrel of crude oil. Transport and out-of-pocket refining costs are then subtracted to arrive at netback price.
Note: The gross refining margin for Dubai crude oil refined in Singapore is used a proxy for Asia/Pacific gross refining margins. Similarly, the gross refining margin for Brent crude oil refined in Rotterdam is used as a proxy for European gross refining margins.
Source: Energy Intelligence Group, *Oil Market Intelligence* , (June 2004, 2005, and 2006; January 2004, 2005, and 2006, and September 2006), page 12.

[1]The companies included are Amerada Hess Corporation, Anadarko Petroleum Corporation, Apache Corporation, BP p.l.c. (only U.S. operations included), Chevron Corporation, ConocoPhillips Inc., Devon Energy Corporation, Dominion Resources, Inc., EOG Resources, Inc., Equitable Resources Inc., Exxon Mobil Corporation, Lyondell Chemical Company, Marathon Oil Corporation, Occidental Petroleum Corporation, Royal Dutch Shell (only U.S. operations included), Sunoco, Inc., Tesoro Petroleum Corporation, Valero Energy Corporation, and XTO Energy Inc.

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