Financial News for Major Energy Companies, Third 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. Twenty major energy companies[1] reported overall net income (excluding unusual items) of $30.0 billion on revenues of $299.3 billion during the third quarter of 2006 (Q306). The level of net income for Q306 was 20 percent higher than in the third quarter of 2005 (Q305) (Table 1). Net income for Q306 increased primarily as a result of higher crude oil prices, higher U.S. refining margins, increased oil and natural gas production, and higher domestic refinery throughput.

Overall, the petroleum line of business (which includes both oil and natural gas production and petroleum refining/marketing) registered a 23-percent increase in net income between Q305 and Q306. A 15-percent increase in oil and gas production net income augmented a 44-percent increase in refining/marketing net income. All lines of business reported higher earnings in Q306 relative to Q305. (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.)

Energy Price News

The crude oil price of Q306 increased by more than one-tenth relative to the prices of a year ago while the price of natural gas fell more than one-fourth. The U.S. refiner average acquisition cost of imported crude oil increased 12 percent relative to a year ago, from $56.69 per barrel in Q305 to $63.68 per barrel in Q306 (Table 2). (See the current and recent issues of the *Short-Term Energy Outlook* for explanation of these price changes.) This was the seventeenth 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 fell 26 percent between Q305 and Q306 from $7.89 per thousand cubic feet to $5.82 (Table 2). (See the current and recent issues of the *Short-Term Energy Outlook* for explanation of these price changes.) This price decline ended a streak of nine consecutive quarters in which natural gas prices increased or were unchanged relative to their year-earlier levels.

Worldwide Petroleum Earnings

Earnings from worldwide oil and natural gas production operations (i.e., upstream operations) increased 15 percent between Q305 and Q306. The increase in foreign earnings augmented an even larger (in terms of both nominal and percentage changes) increase in domestic earnings.

Overall earnings for domestic upstream operations in Q306 were 24 percent higher than in Q305 (Table 1). Domestic upstream earnings increased relative to a year ago due to the effects of higher crude oil prices (Table 2) and essentially unchanged crude oil production. A 6-percent increase in domestic natural gas production by those U.S. majors reporting crude oil and/or natural gas production (Table 1) further enhanced domestic upstream earnings. The results were mixed as slightly more than half of the thirteen companies that reported separate income for domestic upstream operations recorded higher earnings than a year ago. Higher earnings were attributed to increased commodity prices that were magnified by higher production levels (due to acquisitions and recovery from Hurricanes Katrina and Rita). The balance of the companies reported lower earnings, citing lower production levels (due to field shutdowns, mature field declines, and divestitures), higher operating costs, and lower U.S. natural gas prices.

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)

	Q305	Q306	Percent Change[b]	2005	2006	Percent Change
	Financial Data (Millions of Dollars)		(%)	(Millions of Dollars)		(%)
Corporate						
Revenue (20)[c]	290,670	299,331	3.0	786,344	870,357	10.7
Net Income (20)	24,944	30,011	20.3	65,930	83,384	26.5
Worldwide Lines of Business Net Income						
Petroleum (22)	29,860	36,679	22.8	82,432	103,467	25.5
Oil and Gas Production (18)	21,809	25,068	14.9	62,646	74,695	19.2
Refining/Marketing (11)	8,051	11,611	44.2	21,256	28,772	35.4
Gas and Power (10)	874	1,415	61.9	3,451	4,523	31.0
Chemicals (8)	259	2,201	749.5	5,078	5,877	15.7
Domestic Net Income						
Oil and Gas Production (13)	8,437	10,440	23.7	25,398	29,033	14.3
Refining/Marketing (11)	5,855	9,118	55.7	15,877	22,760	43.4
Foreign Net Income						
Oil and Gas Production (5)	7,648	8,971	17.3	21,965	28,191	28.3
Refining/Marketing (5)	2,196	2,493	13.5	5,379	6,012	11.8
	Operating Data					
Oil Production	(Thousands of Barrels/Day)		(%)	(Thousands of Barrels/Day)		(%)
Domestic (17)	3,102	3,087	-0.5	3,424	3,183	-7.0
Foreign (12)	4,731	4,978	5.2	4,801	5,118	6.6
Natural Gas Production	(Million Cubic Feet/Day)		(%)	(Million Cubic Feet/Day)		(%)
Domestic (19)	19,526	20,611	5.6	20,367	20,565	1.0
Foreign (14)	14,628	15,791	7.9	16,290	16,852	3.5
Refinery Throughput	(Thousands of Barrels/Day)		(%)	(Thousands of Barrels/Day)		(%)
Domestic (11)	11,717	12,521	6.9	12,177	12,170	-0.1
Foreign (5)	6,196	6,482	4.6	6,000	6,271	4.5

[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

	Q305	Q306	Percent Change
U.S. Energy Prices[a]			
Refiner Acquisition Cost of Imported Crude Oil ($/barrel)	56.69	63.68	12.3
Natural Gas Wellhead Price ($/thousand cubic feet)	7.89	5.82	-26.2
U.S. Gross Refining Margin ($/barrel)[b]	21.30	24.78	16.3

[a] Energy Information Administration, *Short-Term Energy Outlook* , (Washington, DC, November 7, 2006), 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.

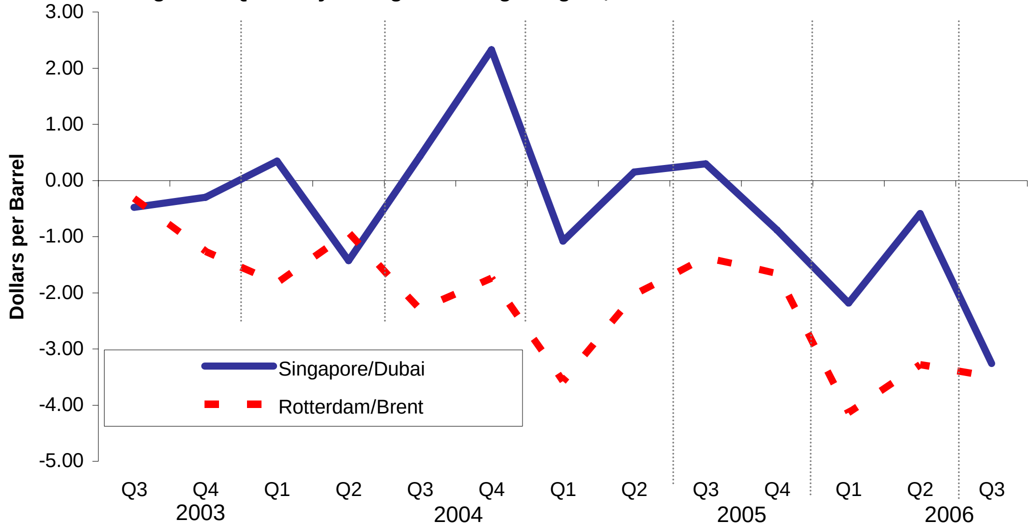
Net income from foreign upstream operations increased 17 percent relative to Q305 (Table 1), as four of the five companies that reported separate net income from foreign upstream operations reported an increase in Q306 relative to Q305. Foreign earnings primarily grew on the strength of higher crude oil prices (Table 2). A 5-percent increase in foreign crude oil production and an 8-percent 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 and natural gas prices and increased production (due to bringing new production on-line, increasing production from existing fields, and asset acquisitions). The company reporting lower earnings from a year ago cited higher taxes assessed on North Sea production as the chief reason for the reduction.

Earnings from worldwide refining and marketing operations (i.e., downstream operations) increased 44 percent between Q305 and Q306 as higher U.S. margins and increased worldwide refinery throughput offset lower industry-wide Asia/Pacific and European refining margins. Higher foreign earnings augmented much higher domestic earnings, resulting in a large increase from $8.1 billion in Q305 to $11.6 billion in Q306.

Profits from domestic downstream operations increased 56 percent in Q306 relative to Q305 as an increase in gross margins was magnified by increased refinery throughput. Motor gasoline stocks were 9 percent lower than in Q305, putting upward pressure on gross refining margins (the per-barrel composite wholesale product price less the composite refiner acquisition cost of crude oil), which increased by 16 percent between Q305 and Q306 (Table 2) Increased domestic refinery throughput relative to Q305 by those U.S. majors reporting domestic refinery throughput (Table 1), which was attributed to recovery from the effects of Hurricanes Katrina and Rita, also put upward pressure on earnings. The net effect of these and other factors was that U.S. refining/marketing earnings increased slightly more than $3.2 billion, to $9.1 billion in Q306 (Table 1). The performance of the eleven companies that reported U.S. refining/marketing earnings was consistent. All of the companies reported higher (or unchanged) earnings in Q306 than in Q305, citing higher refining and marketing margins, greater throughput/utilization rates, trading gains, and lower cost (generally heavier and more sour) crude oil.

Earnings from foreign downstream operations increased 14 percent between Q305 and Q306 (Table 1). Refinery throughput increased by almost 5 percent between Q305 and Q306 (Table 1), but the upward pressure that it placed on earnings was somewhat offset by lower industry-wide margins (Figure 1) in both Europe (by $2.18/barrel) and Asia/Pacific (by $3.56/barrel). The company results were mixed for those companies separately reporting foreign downstream earnings as three of the five reported higher earnings. The companies reporting higher earnings cited higher refining margins and trading gains in their press releases. Alternatively, lower

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.

margins, impairment of assets held for sale, and lower throughput (due to both lower utilization rates and divestitures) provide some explanation for lower earnings.

Worldwide Downstream Natural Gas and Power

Worldwide downstream natural gas and power earnings increased 62 percent (Table 1) due to a variety of factors. Seven of the nine companies reported higher earnings than a year earlier, but for a variety of reasons. Higher earnings were attributed to such varied factors as higher trading earnings, higher NGL prices, reduced fuel (natural gas) costs, reduced storage costs, and the lack of large trading losses. Little explanation was given for lower earnings outside of the lengthy shutdown of a gas plant.

Chemical Operations

Higher margins result in more than a six-fold increase in earnings from the majors' chemical operations. Six of the seven companies reporting results for this line of business recorded higher earnings (or lower losses), resulting in a 750-percent increase in earnings from the majors' chemical operations in Q306 relative to Q305 (Table 1). The higher earnings were chiefly due to Exxon Mobil and BP (i.e., the absence of the large loss that BP's chemical operations generated
in Q305). The foremost reason for higher earnings was higher margins (due to lower natural gas prices). Further, some companies noted higher sales volumes. Alternatively, lower earnings were attributed to lower margins, which were due to higher feedstock costs, and lower sales volumes.

[1]The companies included are Amerada Hess Corporation, Anadarko Petroleum Corporation, Apache Corporation, BP p.l.c. (only U.S. operations included), Chesapeake Energy Corporation, Chevron Corporation, ConocoPhillips Inc., Devon Energy Corporation, Dominion Resources, Inc., El Paso Corporation, EOG Resources, Inc., Equitable Resources Inc., Exxon Mobil Corporation, Kerr-McGee Corp., 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, Williams Companies, Inc., and XTO Energy Inc.

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