



America's Oil and Natural Gas Industry
Putting Earnings into Perspective

December 2008

What consumers are paying for at the gasoline pump



Source: Average of gasoline components from January through September 2008 as reported by EIA.

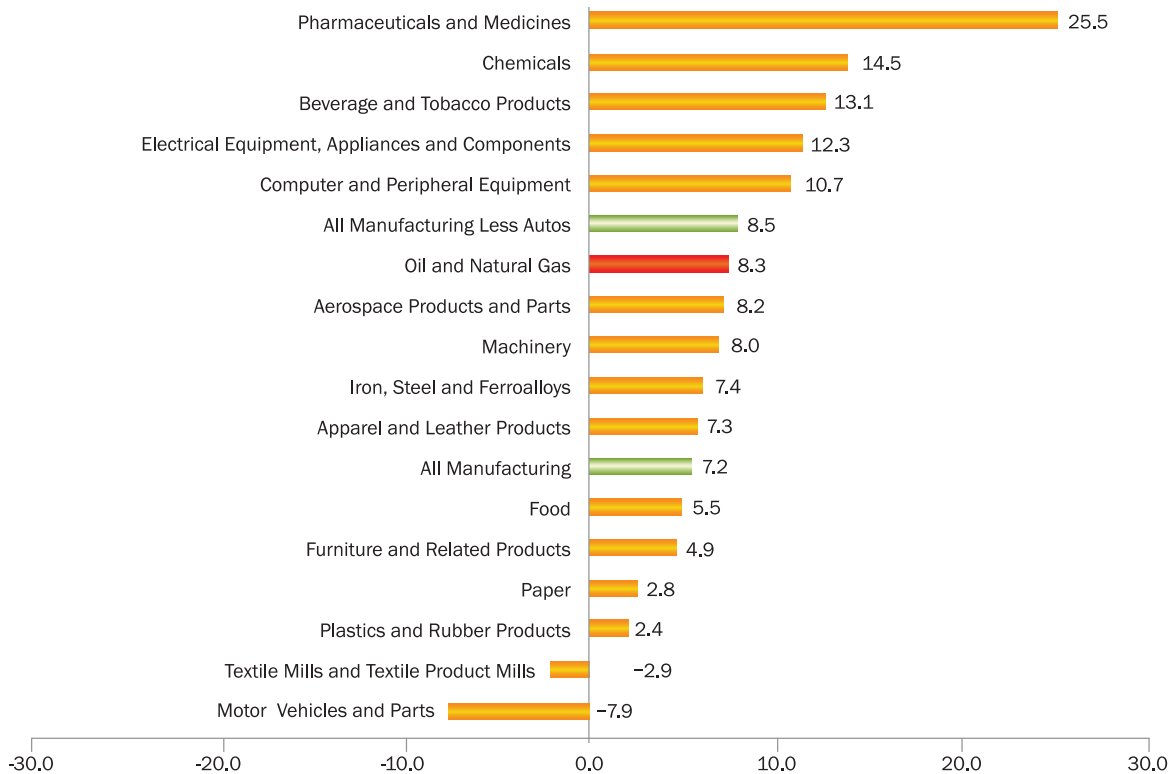
*Earnings differ by company. Figure represents average for the first 9 months of 2008 industry earnings for every dollar of sales calculated from data reported by *Oil Daily*.

Pump Prices: A Fractional Story

The biggest single component of retail gasoline prices is the cost of the raw material used to produce gasoline – crude oil. For example in the first three quarters of 2008, crude oil alone made up 72

percent of pump prices. Refining the crude oil into gasoline and retailing added another 17 percent to the retail price of gasoline. Taxes accounted for 11 percent of the price of gasoline.

First 3 Quarters of 2008 Earnings by Industry (net income/sales)



Sources: Based on company filings with the federal government as reported by U.S. Census Bureau and *Oil Daily*.

Earnings: How Do They Compare?

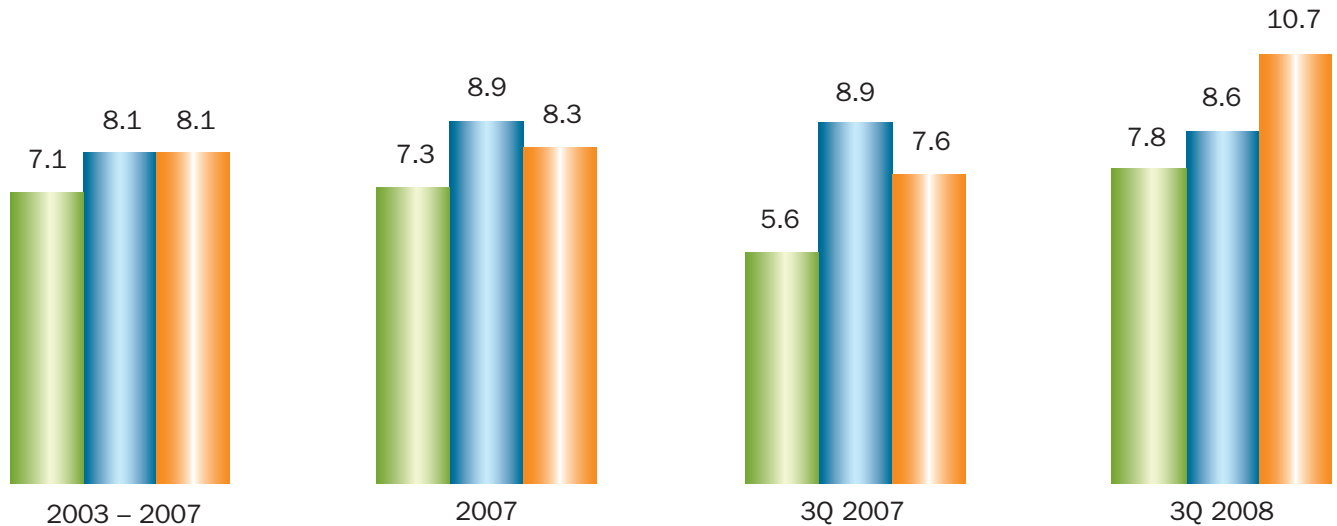
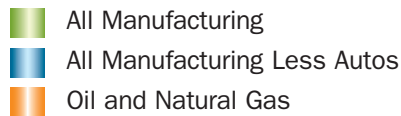
It may seem surprising that oil and natural gas earnings are typically in line with the average of other major U.S. manufacturing industries. This fact is not well-understood, however, in part because reports usually focus on only half the story—the profits earned.

Profits reflect the size of an industry, but they're not necessarily a good reflection of financial performance.

Profit margins, or earnings per dollar of sales (measured as net income divided by sales), provide one useful way to compare financial performance among industries of all sizes.

The latest published data for the first three quarters of 2008 show the oil and natural gas industry earned 8.3 cents for every dollar of sales compared to 7.2 cents for all U.S. manufacturing and 8.5 cents for U.S. manufacturing, excluding the financially challenged auto industry.

Earnings (cents per dollar of sales)



Source: U.S. Census Bureau for U.S. manufacturing and *Oil Daily* for the oil and natural gas industry.

Earnings: Keeping America Going Strong

Like other industries, the oil and natural gas industry strives to maintain a healthy earnings capability. It does so to remain competitive and to benefit its millions of shareholders, across the country and in all walks of life. Healthy earnings also allow the industry to invest in innovative technologies that improve our environment and increase production to keep America going strong—even as it leads the search for newer technologies, and new sources of energy that will provide a more secure tomorrow.

From 2003 to 2007, average earnings for the oil and natural gas industry stood at approximately 8.1 cents on each dollar of sales—a penny above the five-year average of all U.S. manufacturing industries and

equal to all U.S. manufacturing excluding autos. For 2007, the industry's annual earnings averaged 8.3 cents on each dollar of sales, or 0.6 cents below all manufacturing excluding autos. The average for all manufacturing industries was 7.3 cents or a penny lower.

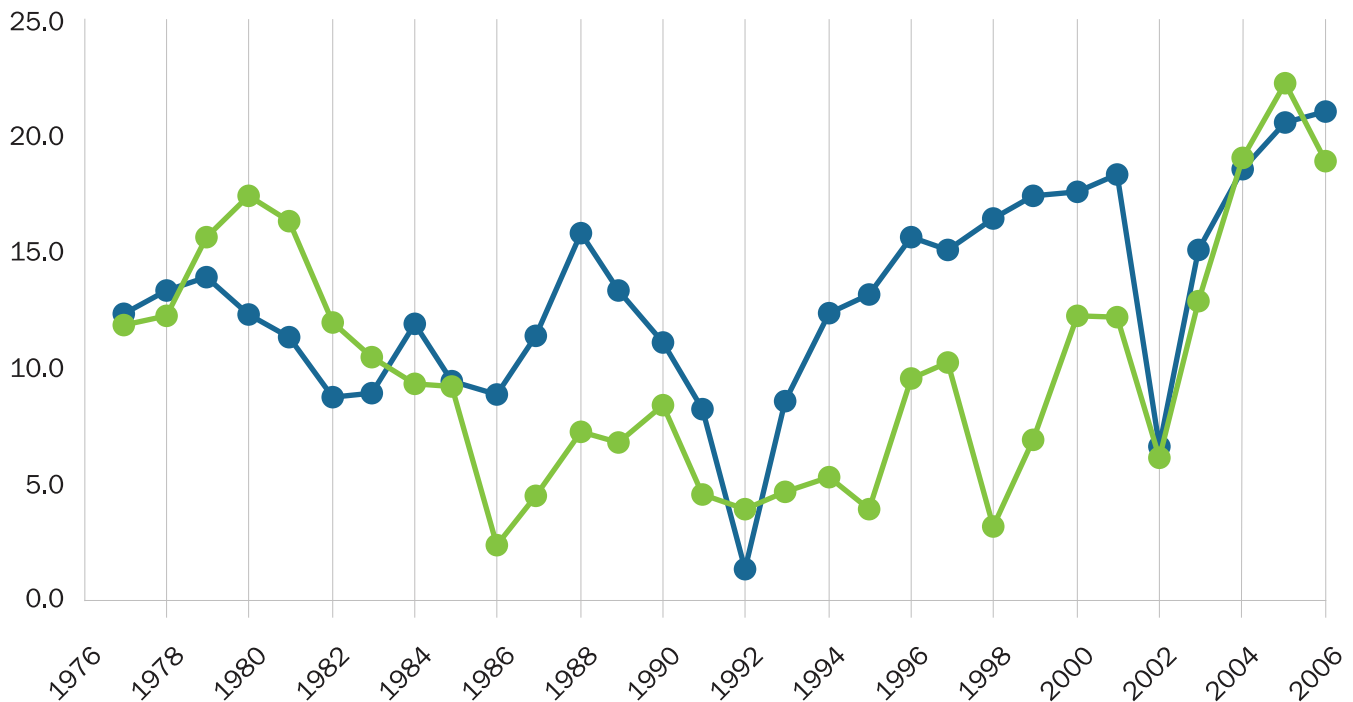
For the third quarter of 2008, the earnings of the oil and natural gas industry were up compared to the third quarter returns of 2007 and compared to the most recent five year period ending in 2007.

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Return on Investment (net income/net investment in place)

—●— S&P Industrials —●— U.S. Oil and Natural Gas



Source: EIA, *Performance Profiles of Major Energy Producers*, various issues and 2006 S&P figure compiled by PWC from Compustat data.

Where our investments are going

Because the oil and natural gas industry is massive and requires huge investments, its earnings contribute greatly to the American economy and way of life. They allow companies to reinvest in the facilities, infrastructure and new technologies that keep America going strong well into the future while generating returns that meet shareholders' expectations.

The oil and natural gas industry is probably one of the world's largest industries. Its revenues are large, but so are its costs of providing consumers with the energy they need. Among those are the cost of finding and producing

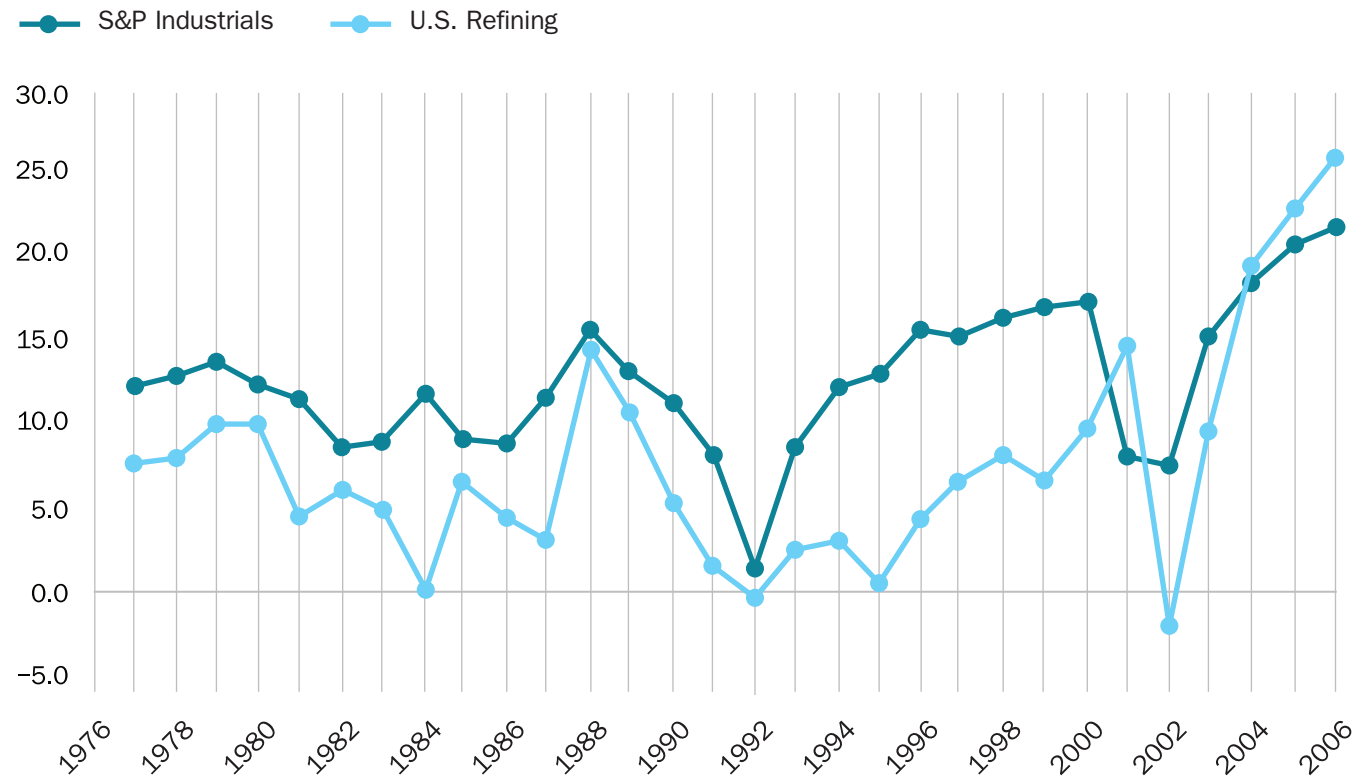
oil and natural gas and the costs of refining, distributing and marketing it. These costs remain huge, regardless of whether earnings are high or low – as was the case throughout most of the 1990s and during other industry "bust" periods.

It is only in recent years that the return on investment (net income/net investment in place) for the industry has matched or exceeded the returns for the S&P Industrials.

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Source: EIA, *Performance Profiles of Major Energy Producers*, various issues and 2006 S&P figure compiled by PWC from Compustat data.

Refining Investments and Returns

Investments in new capacity and improved technologies have enabled U.S. refiners to produce record amounts of fuels for consumers. However, for many years the rate of return on investment in U.S. refining lagged behind the returns for the S&P Industrial average. It is only in recent years that refiners have enjoyed higher average earnings. Refiners need to continually invest, and do so even when earnings are lower.

While no new refineries have been built since 1976, the industry has added the equivalent of one new average-sized refinery each year over the last decade.

Since 1985, refining capacity has increased by 12 percent even though we have 73 fewer refineries. It has been more

efficient to expand at existing refineries because the infrastructure to bring crude in and get products out is in place, the permitting process is quicker, and it is more cost-effective to add on to a refinery versus building a new one. In addition, the elimination of subsidies under the government price and allocation controls in 1981 led to closure of many smaller, less efficient refineries through the 1980s and 1990s.

Capacity has increased while at the same time, industry invested \$88 billion since 1990 to make the cleanest burning fuels in the world. Much of the investments were in technologies and investments to meet stringent clean air standards set by the Clean Air Act of 1990.

Oil and Natural Gas New Investments and Earnings



Source: Ernst & Young

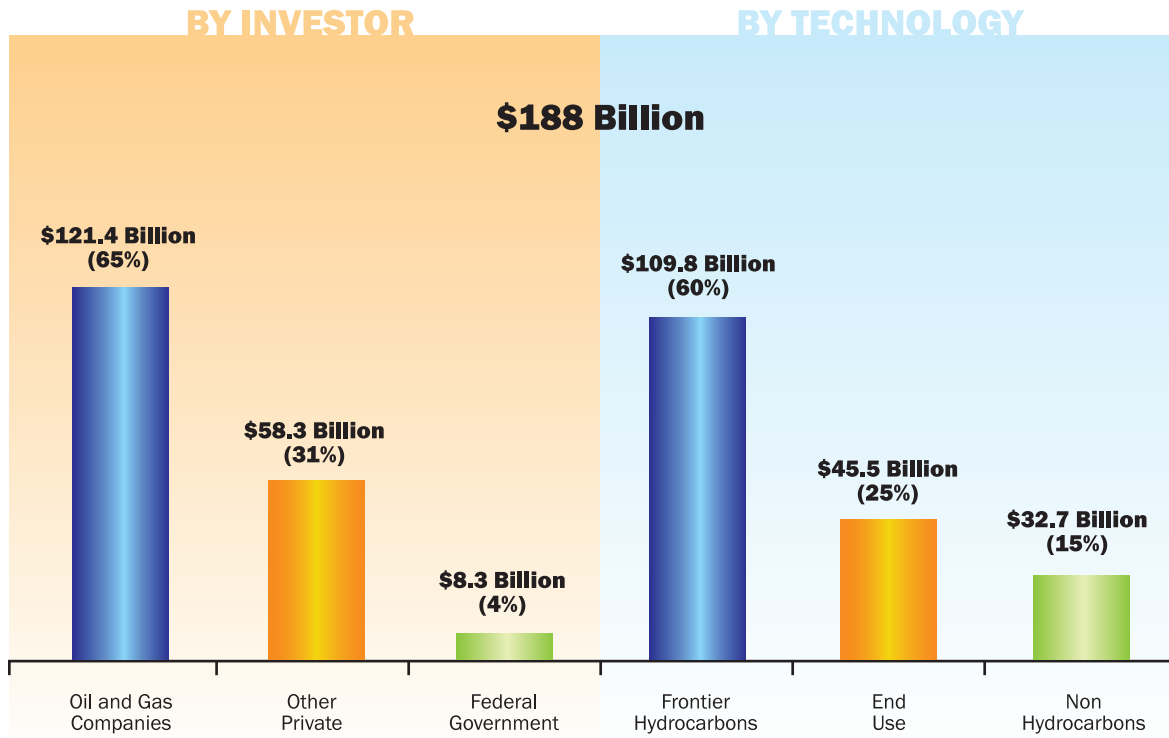
How investments today pay off tomorrow

Today's earnings are reinvested for tomorrow's energy needs. The energy Americans consume today comes from industry investments made years or even decades ago.

Between 1996 and 2007, the U.S. industry invested more than \$1.2 trillion in a range of long-term energy initiatives compared to net income or earnings of \$974 billion.

Investments either planned or currently under serious consideration will boost domestic refining capacity by 800,000 barrels per day over the next three years (2008 to 2010), the equivalent of four new, medium-sized refineries.

Technology – Our Industry’s Investments (2000-2007)



Source: T² and Associates and CEE

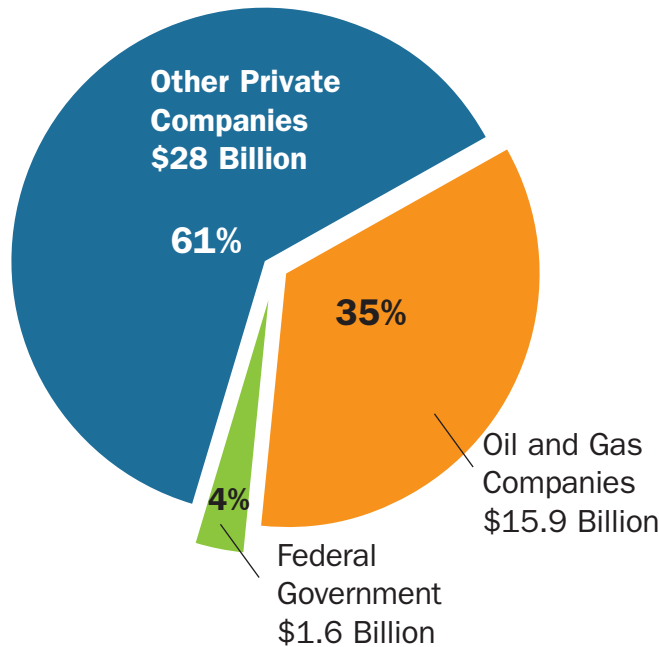
Investments: Securing Our Energy Future

The U.S. oil and natural gas industry invested an estimated \$121.4 billion between 2000 and 2007 in emerging energy technologies including renewables, frontier hydrocarbons, such as shale and oil sands, and end-use technologies, such as fuel cells.

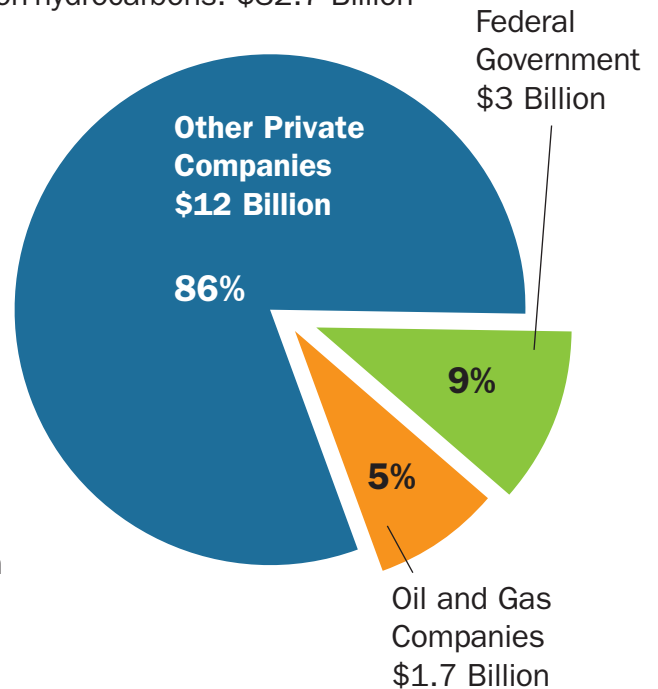
This investment represents 65 percent of the total \$188 billion spent by all of industry and the federal government combined on emerging energy technologies during this time period, according to an October 2008 study by T² and Associates and the Center for Energy Economics (CEE).

Leading Emerging Energy Investments by U.S. Firms (2000-2007)

End Use: \$45.5 Billion



Non-hydrocarbons: \$32.7 Billion



Source: IER and CEE

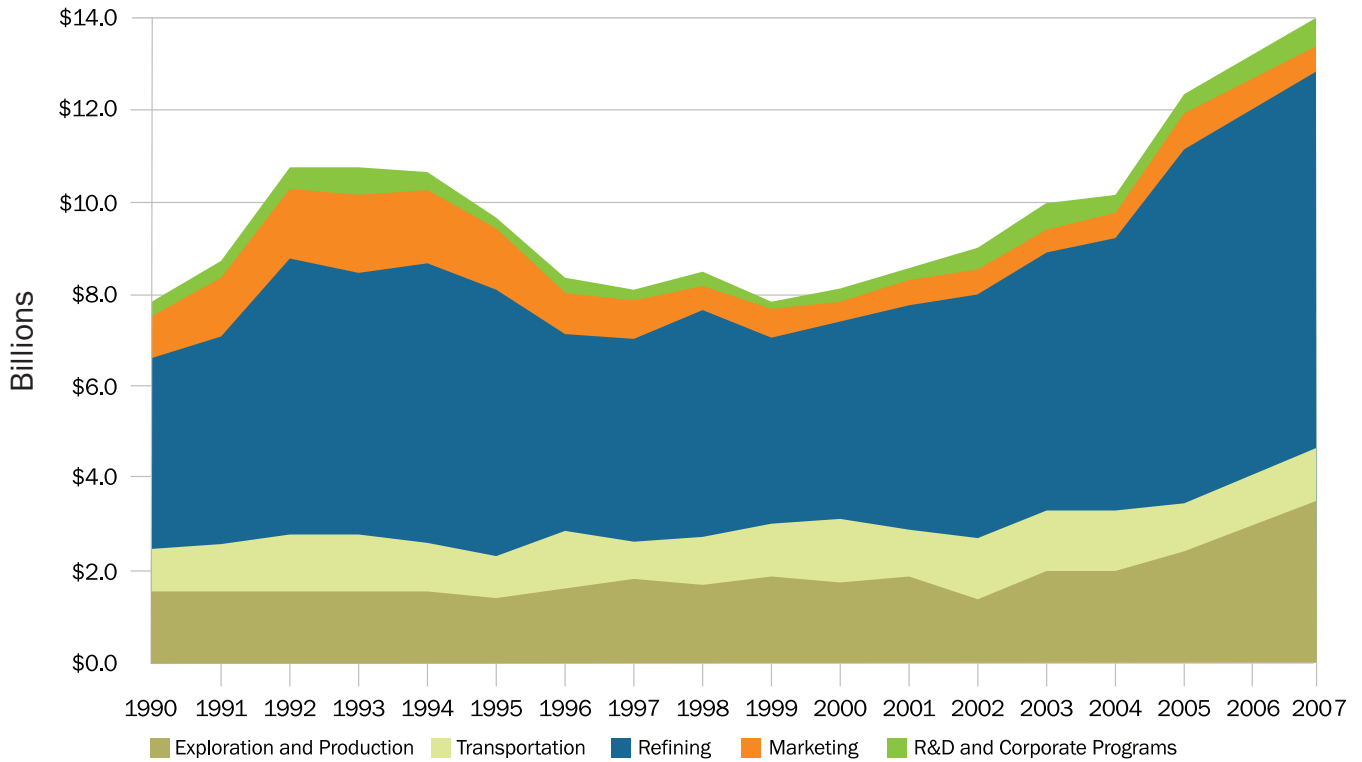
Investing in New and Emerging Technologies

The U.S. oil and gas industry invested \$15.9 billion in the North American market over the 2000-2007 period for advanced end-use technologies, mostly for efficiency improvements through combined heat and power (cogeneration) and for advanced-technology vehicles using fuel-cell technology. Significantly, this \$15.9 billion investment in end-use technologies represents 35% of the estimated total amount (\$45.5 billion) spent by U.S. companies and the Federal government in this area.

Publicly announced non-hydrocarbon investment by the U.S. oil and gas industry is estimated at \$1.7 billion, representing 5% of the total investment of approximately \$32.7 billion. The industry's top investment is in wind with expenditures also made in solar, geothermal, and landfill digester gas.

Total U.S. oil and gas industry end use and non-hydrocarbon investments are estimated to total \$17.6 billion over the 2000-2007 period, or nearly four times the \$4.6 billion invested by the Federal government.

U.S. Environmental Expenditures since 1990 (by sector)



Source: API Statistics, Environmental Expenditures by Oil and Gas Industry, April 2008.

Investing in the Environment

The U.S. oil and natural gas industry has invested more than \$175 billion since 1990 toward improving the environmental performance of its products, facilities and operations; \$582 for every man, woman and child in the United States¹.

In the year 2007 alone, \$11.9 billion was spent implementing new technologies, creating cleaner fuels and funding ongoing environmental initiatives. An additional \$1.9 billion went toward research and development, corporate environmental programs and spill remediation efforts.

¹ Based on U.S. population estimate of 299.4 million by U.S. Census Bureau.



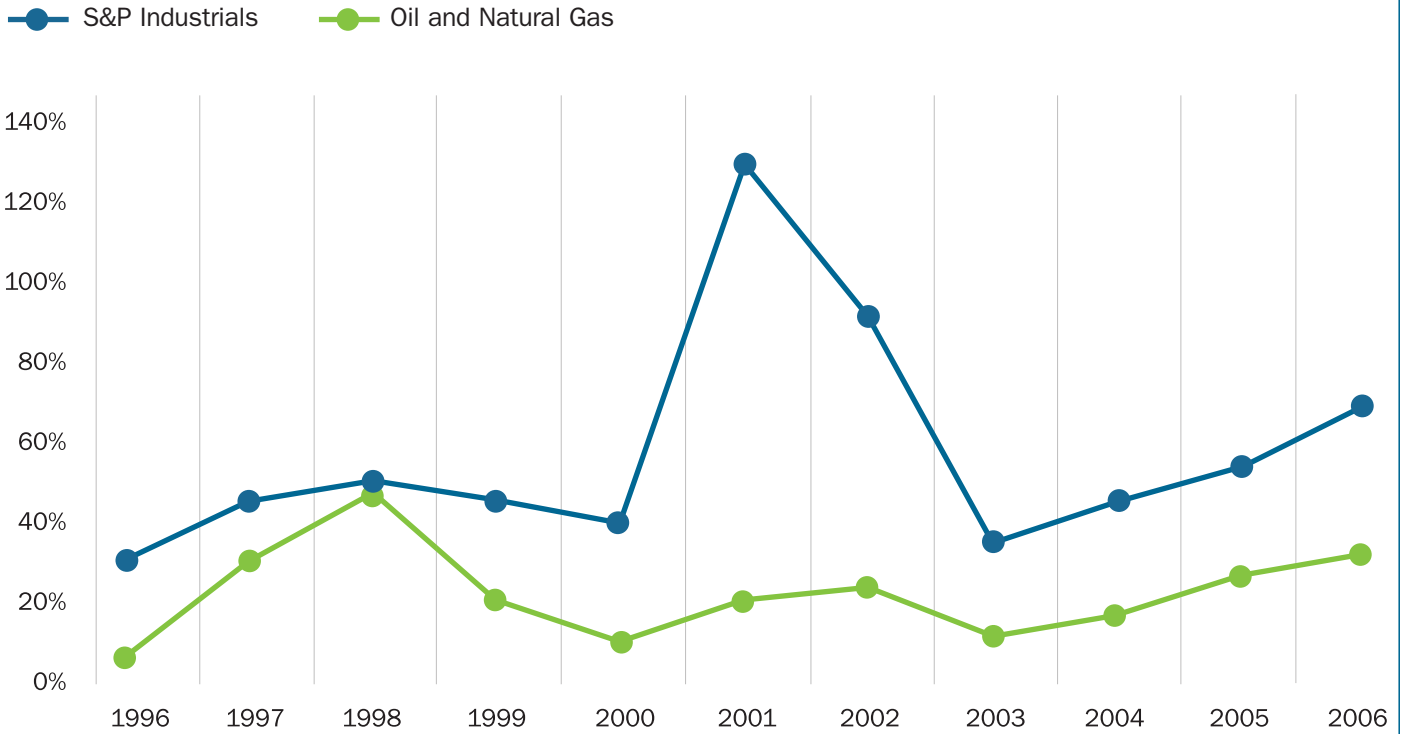
A global business has global expenses

America's oil and natural gas industry is one of the world's most capital-intensive, where companies routinely invest billions of dollars each quarter into exploration, research, development and technology.

A single large offshore platform in the Gulf of Mexico, designed to operate in thousands of feet of water, costs more than \$1 billion to develop – and there are many such platforms worldwide.

Six of the world's 12 largest investor-owned corporations are oil and natural gas companies. Nearly two million Americans work in the industry to ensure that U.S. consumers have the energy they need to continue to improve their quality of life, to further enhance U.S. job creation and to keep our economy growing. Another four million worker's jobs are indirectly tied to the industry. These companies are owned by tens of millions of Americans, who have invested their hard-earned savings on the expectation of a reasonable return on their investment risk.

Stock Repurchases as a Share of Net Income



Source: EIA, *Performance Profiles of Major Energy Producers*

Adding value for shareholders

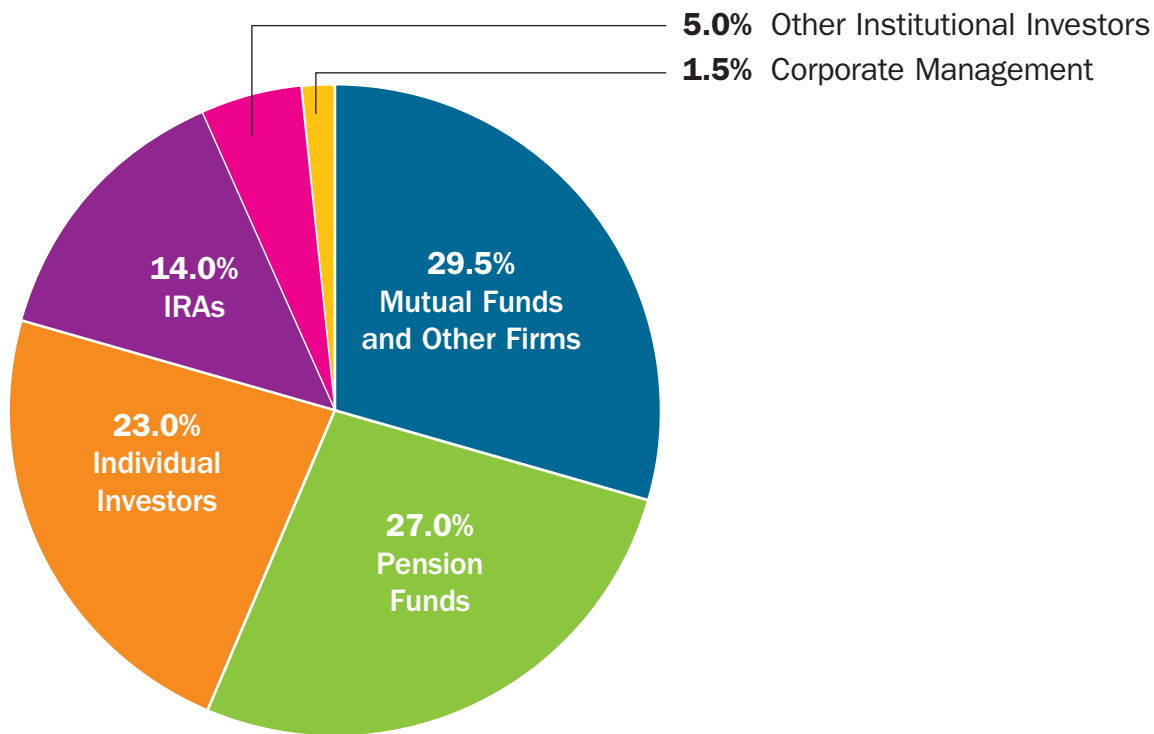
The oil and natural gas industry is very capital intensive and devotes the largest share of its earnings to add new property, plant and equipment to its upstream and downstream operations.

When companies repurchase stock, they are supporting the equity value of the company. This in turn helps the owners of the companies – retirees, future retirees and millions of Americans who have invested their earnings in a secure future.

It is the responsibility of company officials to build value for shareholders; one way to do this is through stock repurchases. Earnings are also used for paying dividends which additionally benefit shareholders.

While the share of stock repurchases in the oil and gas industry has increased in recent years, it is less than half of that for the S&P industrial group. For the last 11 years, the oil and gas industry spent 21 percent of net income on stock repurchases while the rate for the S&P industrials was 52 percent.

Who Owns “Big Oil”? (Holdings of Oil Stocks, 2007)



Source: *The Distribution of Ownership of U.S. Oil and Natural Gas Companies*, SONECON, September 2007

Who owns “Big Oil”?

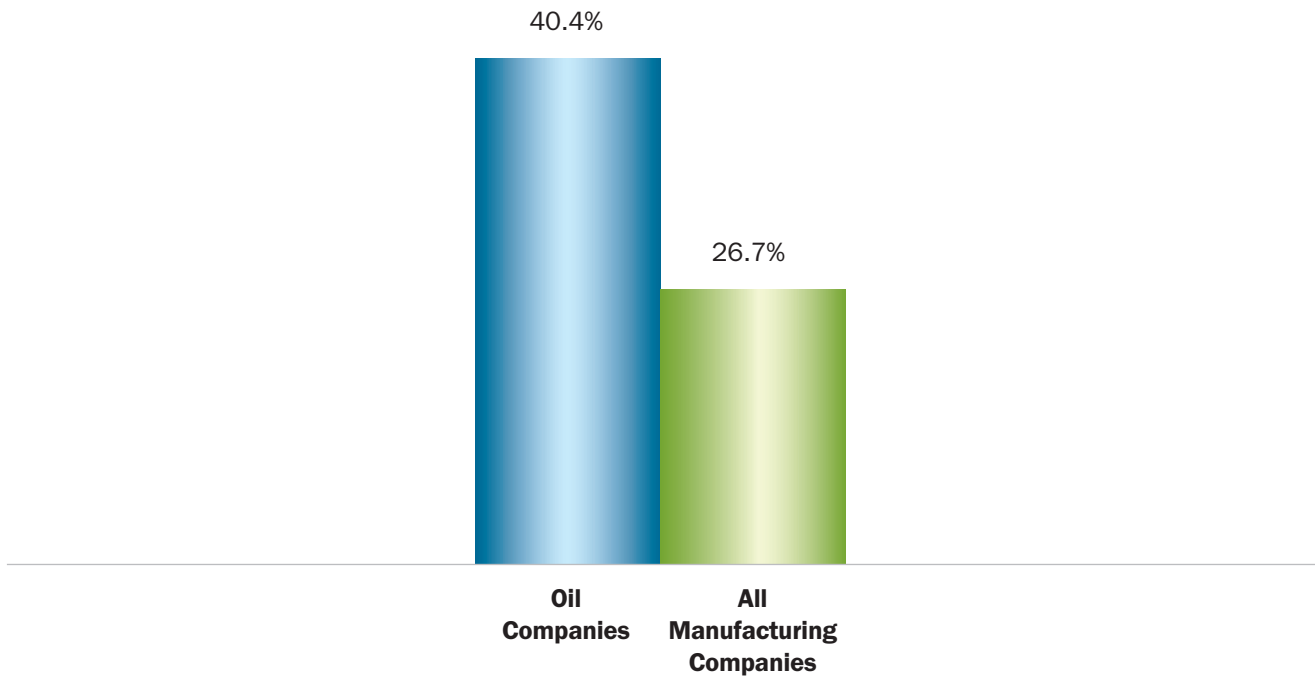
Contrary to popular belief, and what some politicians might say, America’s oil companies aren’t owned just by a small group of insiders. Only 1.5 percent of industry shares are owned by corporate management. The rest is owned by tens of millions of Americans, many of them middle class.

If you’re wondering who owns Big Oil, chances are good the answer is “you do.” If you have a mutual fund account, and 55 million U.S. households do, there’s a

good chance it invests in oil and natural gas stocks. If you have an IRA or personal retirement account, and 45 million U.S. households do, there’s a good chance it invests in energy stocks.

When politicians talk about taxing “Big Oil” or taking their “record profits,” they should think about who would really be hurt.

Income Tax Expenses as Share of Net Income Before Income Taxes, 2007



Source: EIA, *Performance Profiles of Major Energy Producers 2007*

Taxes: Our Industry Pays More

An important part of the revenue earned by U.S. oil and natural gas companies goes to taxes. U.S. oil and natural gas companies pay considerably more in taxes than do manufacturing companies. According to the U.S. Energy Information Administration, the

industry's 2007 income tax expenses (as a share of net income before income taxes) averaged 40.4 percent, compared to 26.7 percent for U.S. manufacturing companies.

¹ Energy Information Administration, *2006 Performance Profiles of Major Energy Producers*, December 2007. These 25 companies accounted for about 44 percent of the total U.S. crude and NGL production, 43 percent of natural gas production, 81 percent of U.S. refining capacity and 3 percent of U.S. electricity. These companies include: Amerada Hess, Anadarko Petroleum, Apache, BP America, Burlington Resources, Chesapeake Energy, Chevron, CITGO Petroleum, ConocoPhillips Petroleum, Devon Energy, Dominion Resources, El Paso, EOG Resources, Equitable Resources, ExxonMobil, Kerr-McGee, Lyondell Chemical, Marathon Oil, Motiva Enterprises, Occidental Petroleum, Shell Oil, Sunoco, Tesoro Petroleum, Total Holdings USA, Valero Energy, The Williams Companies, XTO Energy.

Total Income Tax Expenses (billions of 2007 dollars)



Source: EIA, *Performance Profiles of Major Energy Producers 2007*, Table TS4.

Paying Our Fair Share

According to publicly available data on the top 25 energy companies tracked by the EIA¹, the total income tax expenses incurred by these companies reached nearly \$93 billion in 2006 before falling off slightly in 2007 to \$84.5 billion.

Imposing additional taxes on the U.S. oil and natural gas industry is contrary to the goal of providing stable and cost-effective supplies of energy for American consumers and discourages the tremendous capital investments needed to meet the nation's growing energy needs.

Repeal of tax provisions designed to encourage investment in the United States will discourage new domestic oil production and refinery investments, threaten American jobs, and make it less economic to produce domestic energy resources – thereby increasing our dependence on imported crude oil and gasoline.

Windfall profits taxes do not work because they tax away benefits of better times and offer no help to oil and gas companies during bad times. This discourages investment in domestic production and increases U.S. dependence on imported oil. The Congressional Research Service concluded that between 1980 and 1986 the WPT reduced domestic oil production by as much as 1.26 billion barrels, and increased U.S. reliance on imported oil by as much as 13 percent. Moreover, the oil and natural gas industry is not earning “windfall profits.” The reality is that the industry's earnings have been very much in line with other industries, and often are lower.

¹ Energy Information Administration, *2006 Performance Profiles of Major Energy Producers*, December 2007. These 25 companies accounted for about 44 percent of the total U.S. crude and NGL production, 43 percent of natural gas production, 81 percent of U.S. refining capacity and 3 percent of U.S. electricity. These companies include: Amerada Hess, Anadarko Petroleum, Apache, BP America, Burlington Resources, Chesapeake Energy, Chevron, CITGO Petroleum, ConocoPhillips Petroleum, Devon Energy, Dominion Resources, El Paso, EOG Resources, Equitable Resources, ExxonMobil, Kerr-McGee, Lyondell Chemical, Marathon Oil, Motiva Enterprises, Occidental Petroleum, Shell Oil, Sunoco, Tesoro Petroleum, Total Holdings USA, Valero Energy, The Williams Companies, XTO Energy.

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