S&P Global
Ratings

Industry Top Trends 2022

Oil and Gas

Will The Positive Ratings Trend Continue?

This report does not constitute a ratings action

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What's changed?

Hydrocarbon prices rebounded strongly in 2021, thanks to global economic reopenings, supportive OPEC policies, and ongoing production discipline from North American producers. In some regions, natural gas prices reached record levels.

Environmental, social, and governance (ESG)/Energy transition Last year will be remembered for the acceleration and more widespread adoption of stricter environmental regulation and climate change policies at the company as well as sovereign level. It will also be remembered for successful ESG shareholder activism by some companies' board of directors.

Healthy levels of mergers and acquisitions (M&A) in North America. Most companies completed transactions largely using equity and adhered to a conservative financial policy.

What are the key assumptions for 2022?

Oil and natural gas prices should remain supportive for maintaining the industry's credit quality. If COVID-related economic effects improve, demand in the second half could outstrip supply and lead to higher prices.

Expect issuers to focus more on shareholders with the industry largely restoring its balance sheet.

Global refining to continue to recover in 2022, with less planned downtime and utilization remaining in a narrow band.

What are the key risks around the baseline?

How will supply respond? Any disagreements between OPEC+ countries or a significant shale production ramp-up could lead to more volatile oil prices.

COVID. The potential for more serious mutations of the virus and the implications of further lockdowns remain a threat.

Accelerated energy transition and regulations. Tighter climate change regulations, carbon tax increases, and stringent legislation could result in higher costs, capital reallocation, and less access to capital markets.

Ratings trends and outlook

Global Oil and Gas (excluding Midstream)

Chart 1

Ratings distribution by region

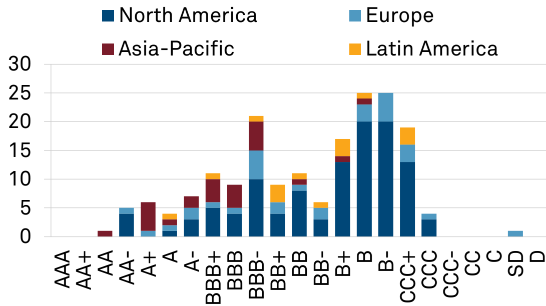


Chart 2

Ratings distribution by subsector

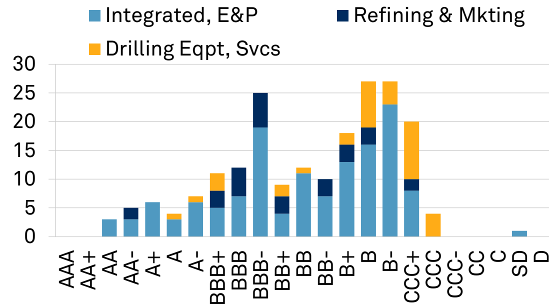


Chart 3

Ratings outlooks

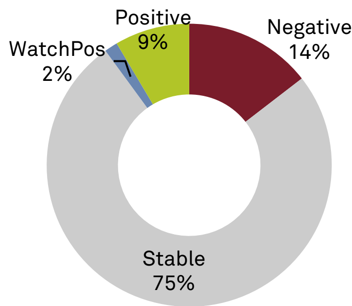


Chart 4

Ratings outlooks by subsector

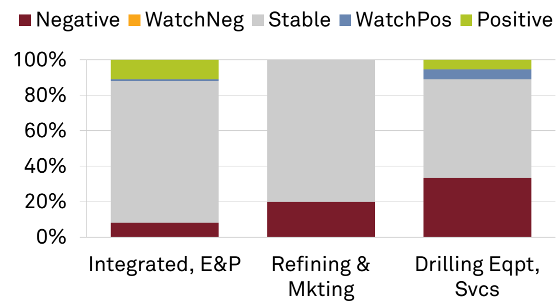


Chart 5

Ratings outlook net bias

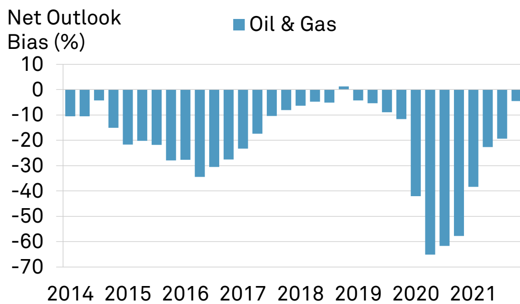
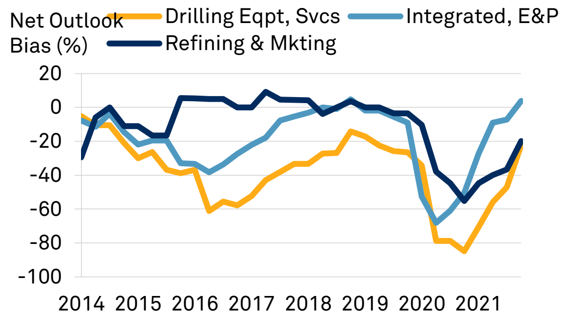


Chart 6

Ratings net outlook bias by subsector



Source: S&P Global Ratings. Ratings data measured at quarter end.

Global oil and gas

Ratings trends and outlook

The ratings for many oil and gas producers clearly benefitted from the recovery in hydrocarbon prices, which allowed public companies to not only generate healthy credit metrics, but to deliver on debt reduction and repair balance sheets.

A dichotomy in our ratings landscape has emerged since the beginning of 2021. For investment-grade issuers to warrant an upgrade, we want to see permanent debt reduction and not just improvement in credit metrics through higher hydrocarbon prices. Typically, for the independent and integrated oil and gas companies, we look at ratios over a three- to five-year period and, with our price deck declining in the later years, debt reduction was necessary to improve metrics and establish a record indicating these improved credit metrics were sustainable. For speculative-grade issuers, we expect ratings to be more volatile relative to their investment-grade peers and improved credit metrics were largely the reason for the majority of upgrades.

Rating actions in the oilfield services (OFS) segment were largely outlook revisions to stable from negative. Unlike their exploration and production (E&P) counterparts, OFS issuers did not enjoy the same degree of benefits from higher oil and gas prices because E&P capital budgets remained relatively restrained. Private sector spending has increased significantly but as an overall percentage of capital spent in North America, it was not sufficient to garner higher prices and margins that would spur upgrade momentum in the OFS segment.

There was a significant uptick in M&A in 2021. Most of the activity involved low-premium transactions that were conservatively financed using a high degree of equity. We believe this is an indication of management's adoption of fiscal discipline under the auspices of investors who will continue to punish companies that lever up or outspend cash flow. The pace of M&A activity will likely slow somewhat in 2022 as more companies consider tuck-in acreage acquisitions to supplement their portfolios

The outlook for ratings remains largely stable with the majority of balance sheets in a much better position. Despite what we expect to be credit-friendly hydrocarbon prices in 2022, we do not expect the magnitude of rating activity in 2022 to mirror that of 2021. This is largely due to the limited ability to reduce debt further, increased use of free cash flow for shareholder initiatives, and increased capital budgets as the sector has largely underinvested over the past couple of years. We expect a 15%-20% average increase in capital spending this year in North America, owing partly to rising inflation costs, which we expect to average 10%-15%. Globally, capital spending will likely increase 10%-15%.

Main assumptions about 2021 and beyond

1. Hydrocarbon prices should likely be supportive of credit quality

The global backdrop for oil remains supportive of the industry's credit quality, with demand gaining momentum as economies continue to reopen, provided the fallout from the pandemic remains manageable or subsides. After OPEC completes its policy of bringing back 400,000 barrels of oil per day (mm/bpd) per month of offline production until it offsets the nearly 10 mm/bpd cut in 2020, it will have limited spare capacity, and tight global inventory will continue to support prices. How shale oil producers respond will remain key to prices in the latter half of 2022. We expect natural gas prices to be more volatile with much of the outlook largely determined by winter weather in the northern hemisphere and the status of the Russia's Nordstream 2 pipeline into Europe. We expect global inventories to remain tight.

2. Expect greater focus on shareholder rewards

We believe the majority of debt-reduction initiatives occurred in 2021 and the focus among integrated and independents will be to keep generating free cash flow but with an emphasis on utilizing it for shareholder initiatives and capital returns. We still believe issuers, by and large, will be adverse to increasing debt leverage, given lessons learned in previous cycles and investor disdain for increased debt and negative free cash flow. Producers will continue to remain disciplined in their capital spending. Reinvestment ratios will nominally increase largely due to inflation, previous underinvestment, and as companies tap less productive reserves given high oil and natural gas prices.

3. Refining profitability will increase

We believe refining margins in most regions will improve as demand recovers and outpaces supply and utilization runs that will likely remain below pre-pandemic levels. The U.S. market is set to rebound with stronger demand and higher margins and lower renewable identification number (RIN) prices. We expect U.S. refiners to chip away at higher debt burdens, which they used to bolster liquidity when demand fell in 2020 and 2021. We also believe shareholders could benefit from a return of capital if balance sheets strengthen. Latin America will likely see mixed results due to more systemic operating challenges and possible shifts in political views. China continues to manage domestic capacity, closing smaller refiners in favor of large, integrated refining and petrochemical complexes and a strong push to electrify the vehicle fleet.

The backdrop for oil prices in 2022 remains supportive largely due to economies reopening and the potential for a return to full demand. The recovery in 2021 as well as OPEC+ curtailments, resulted in a significant drawdown of the surplus created in 2020 to a point where global inventories are approximately 5.5% below the five-year average and 8% below a year ago levels. Barring a more virulent strain of COVID, we expect demand growth to remain strong. However, the supply response and whether it will be sufficient and timely to make up for a possible shortfall in demand remain open questions. The market believes OPEC+ spare capacity is somewhat limited so the questions are: How will North American producers respond as they remain under the watchful eye of investors and will any ramp up in production be meaningful. Moreover, it's still difficult to predict what will happen with the Iranian production, which is offline due to the nuclear-related sanctions. With inventories so tight, any supply disruption or shortfall is likely to be followed by violent price swings.

For natural gas prices globally, we expect prices to remain adequate to support credit quality. Demand should remain strong but much of the price movement will hinge on the winter weather in the northern hemisphere. Given where global inventories are, an

abnormally cold winter will result in gas prices rising sharply higher. Europe relied on imports for 90% of its gas needs in 2019 (as per Eurostat), Europe has seen with a steady decline in production for more than a decade. Much of the price spikes in Europe in 2021 are a result of unseasonable weather patterns, a lack of wind in the North Sea and western Europe, insufficient wind and solar build-out, competitive LNG markets in Asia and Latin America, and the retirement of coal-fired utilities at a pace that was not sufficiently replaced by renewables. Uncertainty surrounding the ramp up of the NordStream 2 pipeline out of Russia (which supplies up to 43% of European gas demand according to Eurostat), continues to weigh on prices. The pipeline has been delayed over German environmental approval as well as growing European discontent with Russia about Russian troops amassing along the Ukraine border. Despite the recent retreat in gas prices in the U.S., prices will likely remain at levels that support credit quality as global LNG demand is expected to remain strong. We don't believe the U.S. will experience the severe shortages seen in Europe. The U.S. is self-reliant for its gas needs and inventory is at comparatively more supportive levels in the event of extreme weather patterns.

The refining industry will continue on the path to recovery, with margins likely to strengthen and utilization stabilizing. While the omicron variant has the potential to dampen demand and lead to lower refining runs, it appears to be having less of an impact on global utilization and demand to date. We think global refining utilization will likely stay in a narrow range of high-70% to low-80% for the first half of the year, and perhaps strengthen if the COVID variants do not lead to more lockdowns. We expect refinery runs and margins to improve overall but remain below 2019 pre-pandemic levels. Another headwind is the planned global capacity increases mainly in Asia and the Middle East. According to Platts, net refining capacity expanded about 1.4 million bpd in 2019 before contracting 400 million bpd in 2020. Expansions resumed in 2021 at about 500 million bpd. We view an increase in crude distillation globally as a negative industry credit factor for 2022.

We expect North American refining credit quality to continue to build on improvements that began in the second half of 2021, as demand came back and margins and utilization improved. We believe utilization will return to the high-80% to low-90% range after seasonal softness in the first quarter and planned turnarounds. We believe the significant amount of rationalization that occurred in 2021 and planned conversions to renewable fuels will boost credit measures and support credit quality. U.S. and Canadian refiners announced about 680 bpd of closures or partial conversions in 2021 and we believe additional capacity could be shuttered in 2022. We think Latin American refinery performance will be mixed, because downtime has remained high due to poor operating performance and low crude inventories in Venezuela. Brazil has been a bright spot with stronger utilization and product demand. Recent political shifts from the presidential elections in Chile and Peru could mean future challenges for operators if policies shift away from hydrocarbons.

We believe China's refineries will experience margin pressure due to lower oil prices and lower demand for refined products as demand moderates. One factor we think will influence demand in 2022 is an increase in new energy vehicle (NEV) sales. China is targeting NEV sales to account for about 20% of all new car sales by 2025, up from about 10% in the first nine months of 2021. We believe China's oil demand will peak around 2030 as the country looks to meet ambitious carbon-emissions goals. New refining investment is also likely to slow as China intends to cap primary refining capacity at 1 billion metric tons per year by 2025.

Credit metrics and financial policy

With the strong rebound in hydrocarbon prices and production, base cash flow and credit metrics have looked very strong for most issuers and their rating categories. Much of the upstream portfolio resides in the U.S., and with prices well above the approximate average shale breakeven price of $50/bbl, issuer profitability and ability to generate cash has improved considerably. Responding to investor pressure and unlike previous cycles, issuers have remained steadfast in limiting capital spending and generating cash flow for permanent debt reduction and shareholder-value initiatives. The adoption of this “fiscal religion” policy led to a slew of upgrades in 2021 throughout our rated portfolio. We expect further potential for debt reduction but not to the extent we saw in 2021. We also expect issuers to adhere to this fiscal discipline in 2022 by limiting capital spending and production growth.

North American refiners' credit measures are slowly improving, rising from the deep hole they found themselves in when demand and EBITDA plummeted in 2020 and the first half of 2021. While many bolstered liquidity with additional debt, investment-grade issuers did not sacrifice their dividend payments while many speculative-grade peers did. While we viewed this significant use of cash as a negative credit factor, this strategy among larger, higher-rated refiners paid off as demand and margins recovered. While credit measures are still weaker than what we expect during normalized midcycle conditions, we believe metrics will continue to improve in 2022, which we reflected in a number of rating outlook revisions to stable from negative toward the end of 2021. Ongoing improvement will largely depend on sustained positive economic growth globally and stronger, resilient demand. We expect margin improvement but think midcycle margins will remain elusive, likely not returning until 2023.

Key risks or opportunities around the baseline

1. COVID and the threat to global demand

The extent of a COVID-19 resurgence and its ultimate impact on the global economy remains the largest unknown. The omicron variant has brought about a significant surge in infection rates, which has led to sporadic closures and lockdowns and raised the specter of more lockdowns as the highly contagious variant spreads. Travel restrictions and work-from-home mandates have continued to constrain oil demand.

2. OPEC/shale production

OPEC has acted like a swing producer by rapidly taking production offline to keep markets in balance. Along with economic reopenings, it was effective in rebalancing global inventories. We believe OPEC will continue to act rationally. However, there always remains the possibility that OPEC+ compliance will not meet intended targets. There is also the threat that production that is currently offline—largely in Iran and Venezuela—could find its way back to the market if the Biden Administration were to lift sanctions on these countries. In the likelihood global demand outstrips supply, the market will look to shale to make up the shortfall. How shale oil producers respond in terms of the timing and magnitude will remain an uncertainty.

3. Accelerated ESG/environmental transition

New climate change policies and regulations, as well as increases in carbon taxes would put additional pressure on the industry, sooner than we currently assume. We believe under the Biden Administration the energy transition story will continue to accelerate in the U.S. through increasing regulation and setting standards/goals for carbon emissions. What that ultimately looks like and what it means for companies' cost profiles, asset allocation, and capital spending plans, remains unclear.

The energy transition is a darkening cloud for the still well-entrenched oil and gas sector, as science, sentiment, and policies push the world away from fossil fuels. This shift of the global energy complex to more sustainable renewable power sources will take decades given the existing frameworks and assets, and the nature and speed of the changes varies by country and segment, adding to the uncertainty. Nevertheless, climate change and encroachment from renewables are likely going to influence industry supply and demand fundamentals and, of course, prices. The timing of peak oil demand remains uncertain. As substitutes for oil and gas such as electric vehicles or hydrogen become more cost-competitive for end users, adoption by country or demographic could shift substantially. We also note that as investors become more in tune to ESG trends and climate change, capital market access could become more difficult and the cost of raising capital could get more expensive. Moreover, several large public companies recently announced the assignment of board of director seats to individuals with a focus on ESG-related trends. We believe these companies will likely face greater scrutiny from public stakeholders who demand greater disclosure and transparency with regard to ESG factors. It's likely ESG-minded stakeholders and board members will push oil companies to take faster and more aggressive actions to significantly decrease carbon and greenhouse gases. They could also potentially influence these companies to reconsider where they allocate and spend capital. It’s also conceivable that recent court rulings, could hold issuers legally responsible for their role in climate change.

Industry forecasts

Global Oil and Gas (excluding Midstream)

Chart 7

Revenue growth (USD)

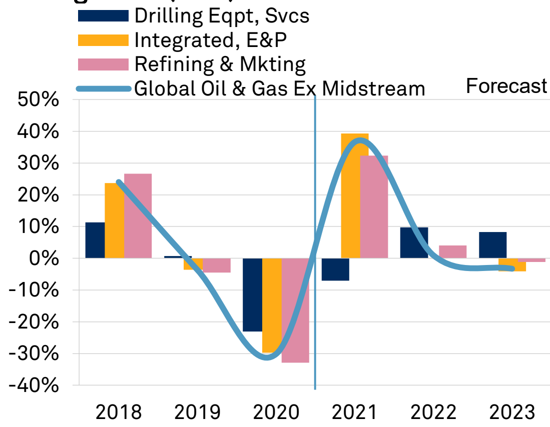


Chart 8

Capex growth (USD, adjusted)

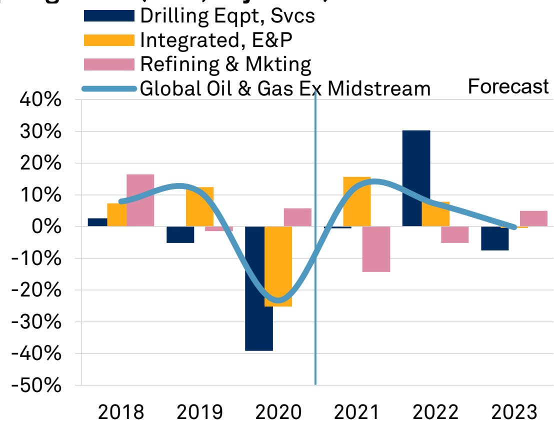


Chart 9

Debt / EBITDA (median, adjusted)

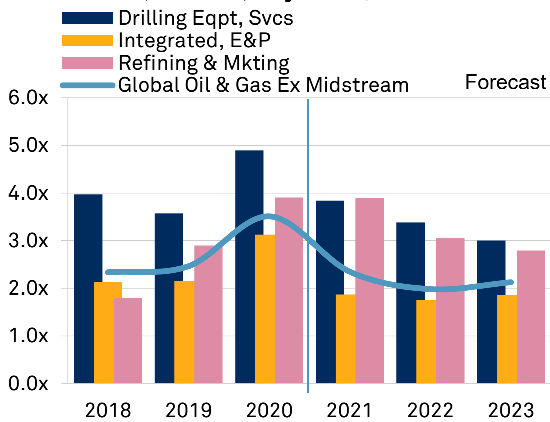
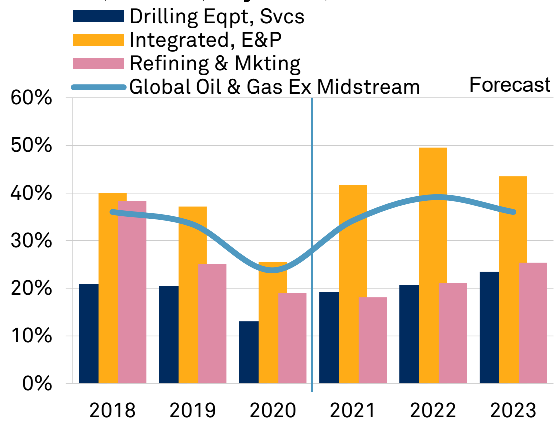


Chart 10

FFO / Debt (median, adjusted)



Source: S&P Global Ratings. Revenue growth shows local currency growth weighted by prior-year common-currency revenue-share. All other figures are converted into U.S. Dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations.

Cash, debt, and returns

Global Oil and Gas ex Midstream

Chart 11

Cash flow and primary uses

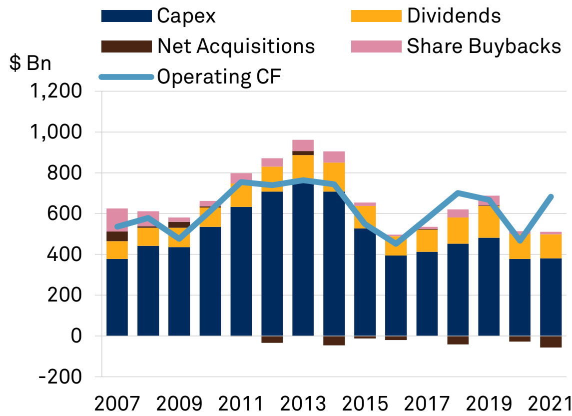


Chart 12

Return on capital employed

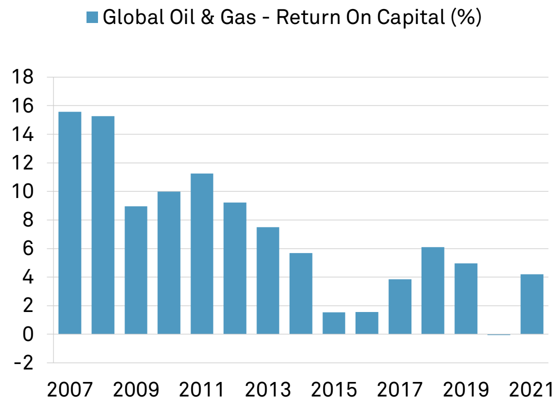


Chart 13

Fixed versus variable rate exposure

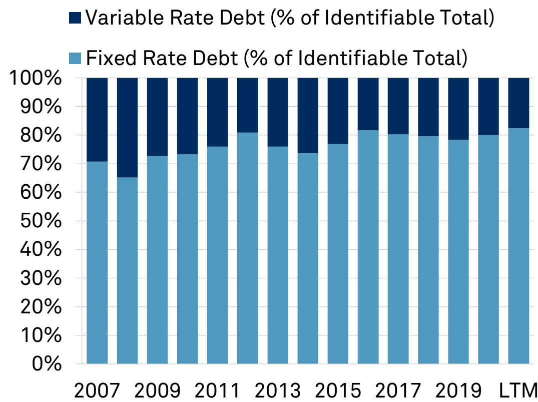


Chart 14

Long term debt term structure

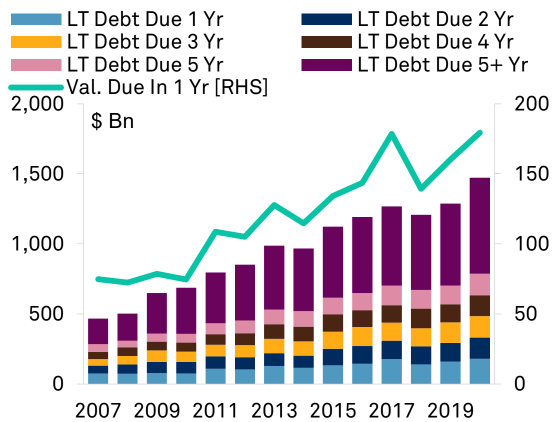


Chart 15

Cash and equivalents / Total assets

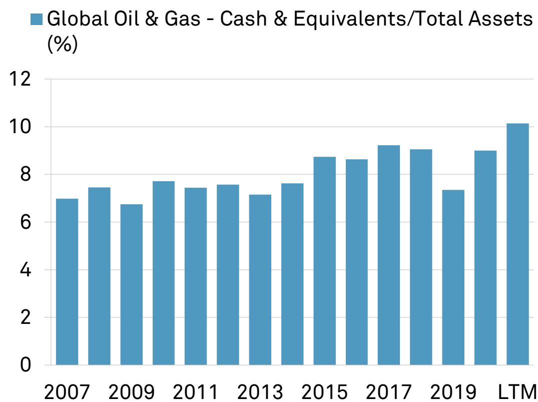
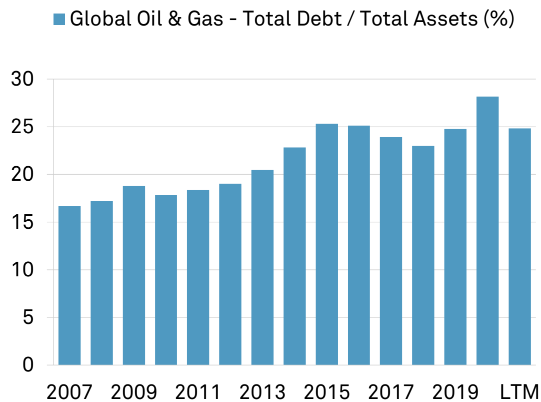


Chart 16

Total debt / Total assets



Source: S&P Global Market Intelligence, S&P Global Ratings calculations. Most recent (2021) figures are using last twelve months (LTM) data

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