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Oil companies suffer climate change setbacks on a historic day for the industry

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Figure 1: The Oil and Natural Gas Industry has come under increasing pressure from investors, regulators and legal precedents to better align with national commitments to decarbonization and disclosure of climate-related financial risks to investors. Source: SciTechDaily (2021).

In a clear signal that the policy environment for companies has already changed and will change even more, the oil industry suffered a series of extraordinary setbacks on May 26 after shareholders, customers and the courts turned on the industry out of concern over climate change.

In the space of a few hours, Exxon Mobil Corp. was thwarted by an upstart shareholder seeking to shake up the company's board; Chevron Corp. Investors instructed the company to cut its greenhouse gas emissions; a Dutch court ordered Royal Dutch Shell to slash emissions by 45 percent, and longtime ally Ford Motor Co. widened its distance from fossil fuels.

The events show that climate concerns, once confined to environmental activists, have become mainstream thinking in the corporate and financial world. The visible effects of climate change, action by governments, and changing consumer sentiment are transforming the world in which oil companies do business.

The pace of these events indicates that companies and oil producing regions are facing less demand for their products. Exxon Mobil, once the largest company in the United States, is now ranked 33rd, and has halved its market capitalization in the past decade.

How the day panned out - Royal Dutch Shell

The action started early on May 26 when a Dutch court ruled that European energy company Royal Dutch Shell had helped drive "dangerous climate change," and ordered the company to cut its own CO_2 emissions and those of its suppliers and customers by 45 percent by the end of 2030 from 2019 levels. The suit, filed by Friends of the Earth Netherlands and more than 17,000 citizen co-plaintiffs, claimed that Shell's annual emissions, which account for about 3 percent of the globe's total, constituted an unlawful danger to the climate that must be stopped.

Shell said last month that it would cut the carbon intensity of its products by 20 percent by 2030 and go to net zero on emissions by 2050, efforts that its shareholders backed last week. The company is also investing billions of dollars in electric vehicles, hydrogen, renewables and biofuels. But the Dutch court said Shell's initiatives were not sufficiently concrete and relied too heavily on "monitoring social developments rather than the company's own responsibility for achieving a CO_2 reduction."

Shell will appeal what it called a "disappointing" verdict, and the ruling sets no precedent for U.S. courts. But the Dutch decision to force emission reductions on a company adds to similar rulings in the Netherlands, France and Germany, in cases that sought to boost government climate efforts. The court is clearly telling the company that they have to make financial sacrifices and change their behavior.

Exxon Mobil

Hours later, Exxon Mobil lost a fight with its own shareholders. Engine No. 1, a small investor group focusing on long-term returns, convinced a majority of shareholders to install at least two of its nominees, Gregory Goff and Kaisa Hietala, on the oil company's board. Engine No. 1 candidate Anders Runevad was not elected, and Exxon said it was reviewing the votes on a fourth, Alexander Karsner. The win by Engine No. 1, though partial, was a milestone and a sign that environmental, social and governance investors are gaining influence in board rooms. The move came despite that fact that Exxon spent $35 million to oppose the effort, and succeeded after BlackRock, the world's largest asset manager with more than $8.6 trillion under management and Exxon's second-largest shareholder, backed three of Engine No. 1's candidates.

Engine No. 1 had argued that Exxon's reluctance to change its business strategy to account for climate change was endangering profits. The vote was a double win for environmentalists and their investor allies: it succeeded only because major asset managers such as BlackRock used their significant clout to force change. Vanguard and State Street, the largest and third-largest shareholders, had not disclosed their votes as of May 26.

BlackRock wrote that "Exxon and its Board need to further assess the company's strategy and board expertise against the possibility that demand for fossil fuels may decline rapidly in the coming decades. The company's current reluctance to do so presents a corporate governance issue that has the potential to undermine the company's long-term financial sustainability." It was a remarkable rebuke to a company that has long held tremendous political sway, including the appointment of its former CEO, Rex Tillerson, to the helm at the State Department in 2017 under then-President Donald Trump.

Chevron

Things went nearly as badly for Chevron, which held its own annual meeting earlier in the day. A shareholder resolution that would force the company to cut its scope 3 emissions — greenhouse gases released by the use of the oil, gas and other products it sells — passed with 61 percent of the vote.

By comparison - Ford

While the oil companies were suffering these setbacks from shareholders, automotive company Ford was expanding its plan to be free of fossil fuels. A week after launching the all-electric F-150, Ford announced that it had already received 70,000 reservations for the pickup truck, which will go on sale in 2022. Ford also increased its spending on electrification, including battery development, to more than $30 billion by 2025 from the current $22 billion. The company anticipates that 40 percent of its global vehicle volume will be fully electric by 2030.

The long-term trend

This series of events is reflective of a longer-term trend towards climate risk disclosures and decarbonization alignment, led by the financial services sector, but now permeating almost every other industrial group. Climate risks are now widely included with more traditional ESG metrics, driven by responsible investing concerns over the past decade, and these expanded metrics are becoming better standardized by regulation and legal precedents.

These recent events highlight how better regulation can ensure that organizations sufficiently disclose the true extent of climate risks to their business, and the level to which the business is aligned with Paris targets, so that shareholders have sufficient information on which to make clear investment decisions. The light will shine increasingly on this area over the coming months in the lead up to COP26 in Glasgow in November.