Shell Disappoints on Weak Oil Refining

By REUTERS

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LONDON (Reuters) - World number three oil company Royal Dutch/Shell reported a 38 percent fall in second-quarter profits on Thursday, at the low end of investor expectations due to weak fuel refining and natural gas returns.

Shares in the Anglo-Dutch group dropped after net profit adjusted to reflect current oil prices fell to $2.202 billion for the three months to end-June. Analysts had forecast $2.45 billion, with estimates in a range of $2.1-2.7 billion.

Weak refining also knocked earnings for the world's biggest oil company, Exxon Mobil, which reported later in the day. Exxon's net profit at $2.64 billion for the quarter was also at the low end of expectations and down 41 percent.

Refining conditions are the ``worst in living memory,'' Shell Chairman Phil Watts told Reuters in an interview. Global refining overcapacity continues to hurt profit margins in producing and marketing fuel, and Shell has been seen as lagging the other big oil firms in improving efficiency in recent years.

“Our second-quarter earnings are below aspirations,'' Watts said in a statement. ``We can do better. We are making progress on our underlying productivity targets, but we have more to do on costs and capital efficiency.''

Shell's shares were down four percent at 418-1/2 pence in London at 1245 GMT, with Royal Dutch 3.5 percent down at 44.95 euros.

Watts later told a news conference the group's three percent a year cost reduction target was proving hard to meet, especially in refining, where costs actually rose three percent in the year so far.

BP CONTRAST

The downbeat outlook contrasted sharply with the confident pronouncements of arch-rival BP earlier in the week, even though BP's 36 percent profits fall was similar in scale.

In the past 12 months Royal Dutch shares have fallen 30 percent compared with a 15 percent fall for BP and 16 for Exxon. Investors see Shell as having worse output growth prospects.

With its Enterprise Oil acquisition, oil and gas production grew eight percent in the half, but underlying growth was only one percent. This compared with BP's 5.5 percent, though the BP figure also includes its increased stake in Russia firm Sidanko.

Analyst Steve Turner of Commerzbank, said the Shell result was “disappointing, but not disastrous,'' pointing to the downstream as the main area at variance with his forecast.

Shell's oil refining and marketing division delivered $347 million in adjusted earnings in the quarter, down from a record $1.035 billion a year ago.

Despite the gloom, most of Shell's shortcomings were now seen to be in the price, especially after the knock its shares took when Royal Dutch was ejected from the S&P 500 index earlier in July.

``It still looks weak in terms of production growth compared with others in the European sector... but the shares are starting to look attractive at these levels,'' said Ignace De Coene, an equity manager at Fortis Investment Management in Brussels.

``The company is very dependent upon crude oil prices, refinery margins and the U.S. dollar and all three worked against them in the second quarter,'' added Lex Werkheim, asset manager at Eureffect brokerage in Amsterdam.

``We are buying today because we don't think those three factors will always work against them. The share is a safe haven, and if the (unstable political) situation in the Middle East escalates, then you have a little bonus.''

Shell Transport, the UK listing for the group, raised its interim dividend 1.7 percent to 5.95 pence, while Royal Dutch increased its payout 2.9 percent to 72 euro cents.

Analysts applauded BP's dividend payout this week, and analyst Peter Hitchens of Cheuvreux said: “I think the dividend should have been higher to show a bit of confidence."

But Shell executives pointed out that in dollar terms for the first half, its dividends were up 15 percent, compared with BP's nine percent.

Many non-U.S. oil firms set their dividends in dollars, even though they are paid in the local currency, because their earnings come mainly from dollar-priced oil.

Watts said the group had “got off to a flying start" in integrating recent acquisitions, which include Enterprise in the UK and the U.S. refining businesses Equilon and Motiva.