



## Warning: 1 Risk Energy Investors Should Worry About

### Description

Today, the global energy industry is sitting on 288 billion barrels of recoverable oil. This is a store of wealth valued in the trillions of dollars. But what if the majority of those barrels could never be burned?

#### The one risk keeping Big Oil up at night

Two publications released this week have reignited the carbon bubble debate in the energy industry. **ExxonMobil** ([NYSE: XOM](#)) released a report downplaying the risks of stranded reserves as a result of efforts to combat climate change, and as study released UN's Intergovernmental Panel on Climate Change warned that climate change poses a serious risk to the global economy and political stability.

In response to calls from shareholders, Exxon published two reports outlining its exposure to the so-called carbon bubble. That is the risk that mandated carbon targets could leave its proved oil and gas reserves unburnable and seriously impact the company's value.

The publication is the first time an oil major has detailed the financial impacts of climate policy. In the report the company said, "we are confident that none of our hydrocarbon reserves are now or will become stranded," and added, "it is difficult to envision governments choosing this path in light of the negative implications for economic growth and prosperity that such a course poses."

That view contrasts sharply with the warnings this week from the IPPC, which painted a grim picture of economic and social disruption caused by extreme storms, rising sea levels, and changing weather patterns.

#### How safe is your portfolio from the carbon bubble?

These reports are forcing energy investors to revisit a key assumption: What if most of the reserves booked by the world's energy companies could never be exploited?

As we burn fossil fuels, the world is getting warmer. To avoid the worst impacts of climate change, the IEA calculates that no more than 1,000 gigatons of carbon can be emitted globally by 2050. That's just one-third of the world's currently booked recoverable oil, coal, and gas reserves. Even assuming an

optimistic rollout of carbon capture technologies, most of the world's energy reserves are essentially unburnable.

Any effort to mitigate climate change would have a devastating impact on the energy sector. Last year **HSBC** analysed the effects of carbon emission caps on Europe's oil majors. HSBC calculated that 6% of **BP's** reserves are at risk, 5% of **Total's**, and 2% of **Shell's**. Norway's **Statoil** had the greatest exposure, with approximately 17% of its market capitalization at risk.

However, HSBC finds that a bigger threat to the sector's value comes from lower energy prices that would result from reduced demand for fossil fuels. In that event, Europe's energy majors could lose 40% to 60% of their current market capitalizations.

Predictably, we would expect similar consequences in the Alberta oil patch. Take two companies like **Suncor** ([TSX: SU](#))([NYSE: SU](#)) and **Canadian Natural Resources** ([TSX: CNQ](#))([NYSE: CNQ](#)), for example, which are sitting on 6.9 billion and 8.0 billion barrels of proved and probable reserves respectively. These assets are some of the most carbon intensive on the planet. In a world with strict emission limits, these reserves are essentially worthless.

Energy investors are probably already well aware of these risks. However, most Canadians would be shocked to learn how much carbon exposure they have hidden within their portfolios.

As another example, take the **S&P/TSX Capped Composite Index Fund** (^OSPTSX). This benchmark is probably a good representation of the average equity portfolio. Notably, more than 25% of the index is allocated to the energy sector. Whether you own oil stocks directly or invest in passive index funds, the average Canadian has a huge carbon risk hidden within their portfolio.

## **Foolish bottom line**

Can investors really trust ExxonMobil? After reading through this report, you can't help but feel like the company is burying its head in the sand, understating the real risks posed climate change. Catastrophic losses follow when fundamentally wrong assumptions are made. It's time to revisit the assumption that all of the energy industry's booked reserves can be exploited.

## **CATEGORY**

1. Investing

## **TICKERS GLOBAL**

1. NYSE:CNQ (Canadian Natural Resources)
2. NYSE:SU (Suncor Energy Inc.)
3. NYSE:XOM (Exxon Mobil Corporation)
4. TSX:CNQ (Canadian Natural Resources Limited)
5. TSX:SU (Suncor Energy Inc.)

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