FIIG | Factsheet

BP Capital Markets plc

30 May 2022

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Issuer Outline

BP Capital Markets plc (BP Capital), is the finance entity which is responsible for issuing debt securities and commercial paper for the BP group companies in the United Kingdom.

BP plc (BP, Company) is one of the five largest global integrated oil and gas companies, with market capitalisation of GBP70bn as at 21 March 2022. The majority of BP's profits stem from its extensive global exploration and production with 2021 production at 3.3 million boepd.

The Company's key upstream operations are in the U.S. (30% of total crude and natural gas production), Trinidad and Tobago (14% due to large natural gas reserves), and Africa (Egypt and Angola, 12% combined). BP's downstream activities comprise refining, marketing, and oil and gas trading activities. Its refineries are mostly in the U.S., Germany, and the Netherlands, while petrochemical capacity comes from China, Germany, Belgium, and the U.S.

Sector: Resources
Sub-sector: Oil & Gas
Country: U.K
Ownership: Public

Key Financials (USDbn)

LTM (31 Dec)	2021
Revenue	156.8
EBITDA	23.8
Net Interest Expense	1.6
Total Assets	287.3
Cash	30.7
Debt	69.8
Net Debt/EBITDA	1.5x
EBITDA/Interest Exp.	14.2x

Source: FIIG Securities, S&P Capital

Summary Bond Details

ISIN	Issue Amount	Ranking	Coupon	Coupon Frequency	First Call	Maturity Date
US05565QDU94	USD2.5bn	Subordinated	4.375%[1]	Semi-Annual	22 June 2025 @ 100	Perpetual
US05565QDV77	USD2.5bn	Subordinated	4.875%[2]	Semi-Annual	22 March 2030 @ 100	Perpetual
XS2193663619	GBP1.25bn	Subordinated	4.25%[3]	Annual	22 June 2027 @ 100	Perpetual

[1] Until 22 September 2025 (Reset Date), thereafter the coupon rate resets every five years to the applicable semi-annual five year US treasury rate plus the following margins: 4.036% to 22 September 2030, then 4.286% to 22 September 2045, and 5.036% thereafter.

[2] Until 22 June 2030 (Reset Date), thereafter the coupon rate resets every five years to the applicable semi-annual five year US treasury rate plus the following margins: 4.398% from 22 June 2030 to 22 June 2050, and 5.148% thereafter.

[3] Until 22 June 2027 (Reset Date), thereafter the coupon rate resets every five years to the applicable annual five year GBP treasury rate plus the following margins: 4.17% to 22 June 2032, then 4.42% to 22 June 2047, and 5.17% thereafter

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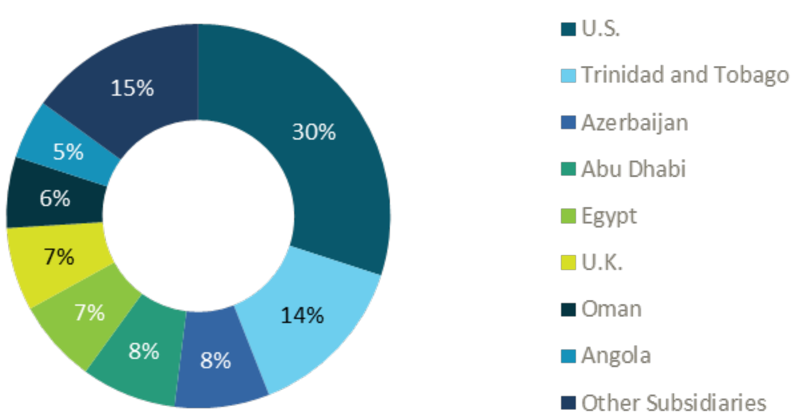
Strengths

- Competitive position: BP is one of the world's largest global integrated oil and gas companies with market capitalisation of USD90bn as at 21 March 2022. BP has large, diversified exploration and production operations and accounts for ~3% of global oil production. The Company is also significantly integrated into downstream operations and invests in renewable energy.
- Geographic diversity of operations: While BP's primary upstream operations are in the U.S., Trinidad and Tobago and Azerbaijan, BP's assets are dispersed over a wide geographic area which covers all large oil basins. BP's downstream activities comprise refining, marketing, and oil and gas trading activities. The Company's refineries are largely located in the U.S., Germany, and the Netherlands, while BP's petrochemical capacity comes from China, Germany, Belgium, and the U.S. S&P commented that BP's direct exposure to emerging markets is lower than that of most of its European peers (with the exception of Royal Dutch Shell).

Figure: 1 – Production by Country (year ended 31 December 2020)



Source: S&P Capital

- Downstream operations: BP has sizable downstream operations that supplement upstream cash flow, especially when the cycle turns. The Company's downstream operations contribute meaningfully to BP's results, in large due to the complex nature of BP's refineries which result in above average profitability in this segment. This, in conjunction with the Company's developing petrochemical, lubricant and retail businesses, add cash flow stability in periods of low oil prices.
- Investment in renewables: For a number of years, BP has been investing in a number of new energy businesses, such as solar, wind, biofuels, and retail energy. While the contribution of these businesses to the Company's consolidated results remains limited, this will likely mean BP is better prepared for the energy transition, which is the main strategic challenge for the oil and gas sector over the next 10-20 years. S&P commented that BP is one of the industry leaders in energy transition, and has aims to become a net-zero emissions company by 2050 or earlier. This implies a reduction of emissions from the current level, of circa 415 million tonnes of carbon dioxide equivalent a year, to net zero.
- Credit metrics improving: In its recent analysis, S&P noted that BP's credit metrics will continue to gradually improve despite lingering pressures from the pandemic. S&P expects FFO to debt above 35% on average, which is a significant improvement from 2020 when this ratio was materially below the threshold of 30%. BP's management of operating costs had historically been weaker than peers', translating into lower profit per barrel and consequently a lower return on capital. However, BP has made significant progress in this area, which should support improved profitability.

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BP’s financial policy provides visibility about uses of cash and balance sheet resilience. During the first nine months of 2021, BP demonstrated adherence to this framework by strengthening the balance sheet. It reduced reported net debt to USD32bn, down USD7bn from the previous year. The interim USD35bn net debt target was reached and retired in early 2021. This, together with further use of free cash for debt reduction, should support credit metrics over the next couple of years, even as and when oil prices weaken.

Under its financial policy, about 40% of surplus cash flow (as defined by BP) is directed to net debt reduction. Importantly, the dividend has been reset at a lower level and protecting the ratings has priority over share repurchases.

- Limited cashflow impact from Russian exit: In late February 2022, BP announced its intention to exit its material (19.75%) stake in Russian-controlled Rosneft Oil Co. PJSC due to the invasion of Ukraine. BP's withdrawal from Russia is a decisive shift in the group's assets, as well as in its exposure to country risk, which is reduced.

  Less favourably, there is no clarity yet regarding how much BP will receive for its stake, although the exit has been announced. Given BP's exit decision and the sanctions imposed on Russia, the value and options available have been reduced. Further, the resulting noncash charges will reduce earnings by up to USD25bn and equity by up to USD14bn. Despite the size of the impairment charge, this is more than compensated by the currently very strong oil price (in excess of USD100) which will boost BP’s operating cash flows by a larger amount than the foregone dividend it would have normally received from Rosneft.

Risks

- Exposure to volatile oil and gas industry: Oil, gas, and product prices are subject to international supply and demand and margins can be volatile. Political developments, increased supply from new oil and gas, or alternative low carbon energy sources, technological change, global economic conditions, public health situations, and the influence of OPEC+, can impact supply and demand and therefore prices for BP’s products. Decreases in oil, gas or product prices could have an adverse effect on revenue, margins, profitability and cash flows.
- Operating cost position: Historically, BP's management of operating costs has been weaker than its peers', which has translated into lower profit per barrel, and consequently a lower return on capital. However, in recent years, BP has focussed on cost reduction. S&P commented that the Company has made significant progress in this area, which should support improved profitability. BP's cash flow breakeven is currently below USD50/bbl, and we note the guidance of USD40/bbl Brent, USD3 Henry Hub and a refining indicator of USD11/bbl over 2022-2025. We believe this should be achievable, based on the quality of BP's upstream portfolio, and the ongoing group restructuring.
- Requirement to replenish reserves: BP is required to constantly renew its reserve base in order to ensure future prospects for the Company. Competition for access to investment opportunities, heightened political and economic risks in certain countries where significant hydrocarbon basins are located, unsuccessful exploration activity and increasing technical challenges and capital commitments may adversely affect the Company’s reserve replacement strategy.
- Environmental, Social and Governance (ESG) concerns: Laws, regulations, policies, obligations, social attitudes and customer preferences relating to climate change and the transition to a lower carbon economy could have an adverse impact on BP’s business (including increased costs from compliance, litigation, and regulatory or litigation outcomes), and could lead to constraints on production and supply and access to new reserves and a decline in demand for certain products. Technological improvements or innovations that support the transition to a lower carbon economy, and customer preferences or regulatory incentives that alter fuel or power choices, could impact demand for oil and gas. Depending on the nature and speed of any such changes, this could adversely affect the demand for BP’s products, investor sentiment, the Company’s ability to access to capital markets, its competitiveness and financial performance.

  BP aims to become a net-zero-emissions company by 2050 or earlier. This implies a reduction of emissions from the current level, of about 415 million tonnes of carbon dioxide equivalent a year, to net zero. We expect that BP's higher exposure to natural gas production, investments in renewable operations, and more active management approach will help the company to achieve this target.

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Risks relevant to the Subordinated notes

- Subordinated position of the notes: The notes are subordinated in all respects to BP Capital's and BP's senior debt. There is no restriction on the amount of securities, guarantees or other liabilities which BP Capital and BP may issue or incur and which rank senior to or equally with the notes. This means that, in the unlikely event that BP were to default, the recovery on the Notes would likely be minimal.
- Resetting interest rate: The interest rate on the notes for each relevant reset period will equal the Five-Year Treasury Rate in plus the relevant reset margin. Therefore, the interest rate after the relevant first reset rate could be less than the fixed rate for the initial period and any interest payable after the relevant first reset date and each subsequent reset date may be less than a prior fixed rate.
- Perpetual maturity: The notes are perpetual securities, meaning that BP does not have any obligation to repay the capital at a future date. As a consequence, holders wishing to recover their capital would need to sell their notes on market, at a price which may be lower than the face value of the notes.
- Rating risk: The notes have been issued in part to support BP's corporate rating. This is because the terms of the notes (subordination, interest deferral, perpetual) results in the rating agencies treating 50% of the notes as equity for the purpose of their financial analysis. Further, based on S&P's current rating methodology, the notes would be treated as 100% debt from their first call date. This current rating construct means that BP would have a significant incentive to redeem the notes at the first possible option. However, should rating agencies change their methodology and provide rating support for a longer period of time, this would remove this incentive to call and would likely result in a (potentially significant) drop in the price of the notes.

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