# Oil & Gas Service Firms Hit by Stalling Activity Levels in Q1

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The oil and gas industry experienced a significant slowdown in Q1, per a recent survey released by the Federal Reserve Bank of Dallas. The bank's business activity index, which assesses conditions faced by oil and gas companies across Texas, Louisiana, and New Mexico, dropped significantly to 2.1 from 30.3 in Q4 2022, indicating a pessimistic sentiment among the firms.

Several companies surveyed also reported rising costs for the ninth consecutive quarter. Additionally, weaker prices for oil and gas have been affecting their cash flow and profits. The average break-even price (or the minimum price required to make profits on a new well), as reported by participants, was $62 per barrel, which is more than 10% higher than the average in 2022.

Consequently, the upcoming earnings season might be challenging for oil and gas service companies like **Halliburton** (HAL - Free Report) , **Core Labs** (CLB - Free Report) and **Schlumberger** (SLB - Free Report) .

Let's delve deeper into the survey results to understand the situation better.

## Pessimistic Sentiment Among Oil and Gas Companies

The Q1 slowdown in the oil and gas industry is not a surprise, considering the weak sentiment among the firms. The global banking industry's concerns led to falling oil prices in March, which may have contributed to the sentiment among the firms surveyed.

## Rising Costs a Major Concern

Rising costs have been a major concern for the oil and gas industry, with several companies reporting an increase in costs for the ninth consecutive quarter. The rising costs are primarily due to the increased demand for equipment and labor, which has led to a shortage of both. As a result, many companies have been forced to pay higher prices for equipment and labor, which affected their profitability.

## Weak Prices of Oil and Gas

Weak prices of oil and gas have also been affecting the cash flow and profits of many companies surveyed. The ongoing pandemic has led to a decline in demand for oil and gas, resulting in a surplus in the market and pulling down prices. Companies have been forced to sell their products at lower prices, which affected their profitability.

## Break-Even Price on the Rise

According to all respondents, the average breakeven price for oil production was $62 per barrel, indicating a significant increase of more than 10% from the previous year's average. The rise in break-even prices is primarily due to the rising costs of equipment and labor. Many companies are finding it difficult to maintain profitability at current prices, and a increase could lead to more companies shutting down their operations.

## Rig Count and Price Relationship

In the week ended Feb 24, the number of oil rigs being used for drilling decreased to 600, a drop from the peak of 627 seen in the week ending on Dec 2. This decline in rig count occurred in five out of the eight most recent weeks and rig count is currently at its lowest point since July 2022. It seems that the increase in drilling activity that began in August of 2020, following the first wave of the pandemic, has either come to a halt or possibly ended.

Historically, there has been a correlation between changes in rig count and fluctuations in front-month WTI futures prices, typically with a lag time of approximately 4-5 months. When there is an increase in oil prices, the delay is due to several factors. These include confirming whether the price level is sustainable or temporary, contracting additional rigs, transporting them to the drilling site, assembling the necessary equipment and starting the drilling process. Conversely, when oil prices decrease, the lag in the response is due to factors such as confirming the downward trend, completing partially drilled wells, drilling wells that were already contracted and shutting down any unnecessary rigs.

At the beginning of June 2022, WTI futures reached the highest point, rising over 70% compared to the same period in the previous year. The highest number of oil drilling rigs was recorded in late November, approximately 25 weeks after the peak in prices, which is slightly longer than the usual period. From June 2022, prices have been decreasing gradually and this has caused a slow but steady decline in drilling activity. Currently, the prices are around 15% lower than a year ago and are still on a downward trend. This suggests that drilling activity is likely to decline until the end of June 2023.

## Production Growth Impacts

After the completion of drilling, there is typically an additional delay of six months on average for various activities such as casing, pressure pumping, installation of surface equipment, flow testing, connection to the pipeline network and start of commercial production. As a result, the current decrease in drilling activity is expected to limit production growth until the end of 2023 and possibly even into 2024.

The slower growth in U.S. production will prevent any buildup of crude oil inventories, even if there is a pullback in the global economy this year. It will also limit the potential for non-inflationary growth for the remaining of 2023, and 2024.

Here are three oil stocks that could be impacted by the Q1 slowdown in the oil and gas industry:

**Halliburton** is a major oilfield services company that provides drilling, completion, and production services to oil and gas producers. This Zacks Rank #3 (Hold) company is headquartered in Houston, TX and has operations in more than 70 countries worldwide. With its close ties to the oil and gas industry, Halliburton may be impacted by the slowdown in activity levels.

Halliburton is set to release first-quarter results on Apr 25. The current Zacks Consensus Estimate for the to-be-reported quarter is a profit of 67 cents per share, indicating a decline from 72 cents in the December quarter.



**Core Laboratories** is a Netherlands-based offshore drilling contractor that specializes in ultra-deepwater and harsh-environment drilling services. This Zacks Rank #3 company operates a fleet of high-specification drilling rigs around the world and provides services to oil and gas companies. A slowdown in the industry could impact Core Laboratories’ business, particularly if oil and gas companies reduce exploration and drilling activity.

Core Laboratories is set to release first-quarter results on Apr 26. The current Zacks Consensus Estimate for the to-be-reported quarter is a profit of 19 cents per share, indicating a decline from 20 cents in the previous three-month period.

**Schlumberger** is another major oilfield services company with operations around the world. This Zacks Rank #3 company provides technology, information solutions, and integrated project management services to the oil and gas industry. As such, its fortunes are closely tied to those of the industry, and a slowdown in activity levels could impact Schlumberger's business.

Schlumberger is set to release first-quarter results on Apr 21. The current Zacks Consensus Estimate for the to-be-reported quarter is a profit of 69 cents per share, indicating a decline from 71 cents in the previous three-month period.

The first-quarter slowdown in the oil and gas industry is not unexpected, considering the pessimistic sentiment among the firms surveyed. Rising costs and weak prices for oil and gas have been major concerns for many companies, affecting their cash flow and profits. Instances of break-even prices have also been on the rise, primarily due to the increasing cost of equipment and labor. Companies must remain cautious and adopt a prudent approach to ensure their long-term sustainability.