

Shell-shocked: a whale trade in corporate bonds

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In “[Big Oil’s terrible day: Bond market \(non-\) reactions](#)”, AFII, 1 June 2021, we argued that the controversy at the time around legal issues for Shell (RDSALN) motivated an underweight on their long-dated USD bonds, more specifically the RDSALN \$3.25 04/50 (US822582CH36) bond.

Since October, the bond has widened significantly from 120bp to >150bp (see Figure 1). Paired with an underwhelming new issue last week, it would be a stretch to call sentiment bullish even if energy markets are buoyant.

To further entrench any cautious views on these bonds, investors need only turn their eyes to the controversy brewing in South Africa (and one without Greek letter connotations). In what seems almost unprecedented action, local petrol stations have started de-franchising themselves from the Shell brand.¹

Why? Shell is starting seismic exploration for oil and gas resources off the East Coast of South Africa. AFII and the IEA may disagree with the company’s urgency to find more oil and gas, and the optics of this so soon after COP26 are not ideal. Regardless, the potential broader implications of seismic surveys on marine life are disconcerting and at the core of ongoing local protests in South Africa.

In exploration studies, air cannons are fired into the sea to generate sound waves whose bounce-backs allow the explorer to triangulate oil repositories (see Figure 2 overleaf). Arguably, the effect on marine fauna – given their highly developed auditory perception – while surveys are conducted could be analogous to the human experience of being “shell-shocked”.

Given Shell's stated ambitious (net zero) transition strategy, we are concerned to see such a project in play and keen to understand how this fits in the strategy. **While awaiting such clarity, we retain our underweight stance on the old as well as the new long-end USD bonds.** This project runs the risk of being counter-productive towards net zero goals considering recent evidence that whales may be one of the more efficient and practical Carbon Capture and Storage (CCS) mechanisms.²

Figure 1. RDSALN 30yr bonds widening last month.



¹ See e.g. “[Shell’s seismic survey fuels call for boycott at the pumps](#)”, Times South Africa, 25 Nov 2021 or “[Shell faces protests over seismic survey plans in South Africa](#)”, Offshore Energy, 23 Nov 2021.

² “[Nature’s Solution to Climate Change](#)”, IMF Finance & Development, Dec 2019, Vol 56:4.

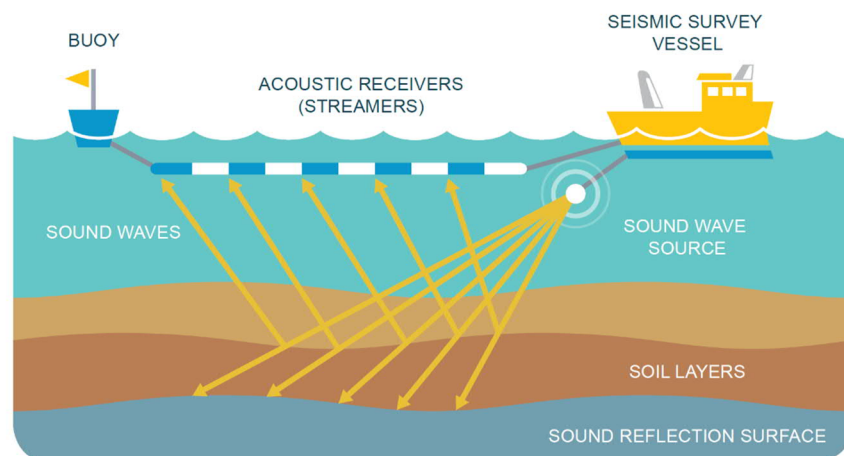
Seismic activities' impact on biodiversity

Seismic surveys aim “to explore the layers of rock below the seabed for geologic features that indicate the presence of oil or gas.”³ Through seismic pulses, survey vessels generate seismic waves that reflect back off the different layers of rock that might be present in the seabed, see Figure 2. Data collected is then processed by geologists to determine the potential presence of petroleum deposits.

There is strong scientific evidence that seismic surveys have a negative impact on marine species, including mammals, fish and invertebrates⁴ although one should recognize that it is not an uncontested conclusion especially on behalf of the oil and gas exploration industry.⁵ Whales seem to be particularly affected, as they rely on acoustic communication for breeding, navigating and finding prey. Coincidentally, the Southern Right whale has its migration pattern along the South African coast right now,⁶ which could pose further problems. South Africa has the third highest level of marine endemism after New-Zealand and Antarctica.⁷

Shell's interest in the particular area follows an acquisition of a 50% working interest and operest of the Transkei & Algoa exploration area. Impact Oil and Gas Ltd holds the other half.⁸ The particular Shell vessel executing the seismic project is called “Amazon Warrior”. Unfortunately this does not mean its mission is set out to protect the Amazon, rather the Norwegian owned vessel's colloquial name is, according to sources, “The Beast.” It is owned and operated by Shearwater GeoServices AS,⁹ who acquired the the vessel and other assets from Schlumberger in 2018.

Figure 2. A marine seismic vessel creates the “pulse” needed to take seismic readings. Source: [New Zealand Government, AFII](#).



³ “[Offshore Seismic Surveying](#)”, New Zealand Government et al., 2018.

⁴ “[A critical review of the potential impacts of marine seismic surveys on fish & invertebrates](#)”, Marine Pollution Bulletin, 2017.

⁵ See for example “[Seismic surveys both increase and reduced \[sic\] fish catches](#)”, Norwegian Petroleum Directorate, 2010.

⁶ “[Eubaleana Australis – The Southern Right Whale](#)”, SA Venues, 2021.

⁷ [National Biodiversity Assessment 2018](#), South African National Biodiversity Institute, 2018.

⁸ “[Shell faces pushback over offshore South Africa seismic survey plans](#)”, World Oil, 29 Nov 2021.

⁹ Ticker GEOVES. The company is private and public information is sparse. Currently, some funding is coming through a loan facility (FIGI BBG00S6S6CL4) provided by Nordea (51%), ABN Amro (20%), Danske Bank (14.4%) and NIBC Bank (14%) established in 2020.

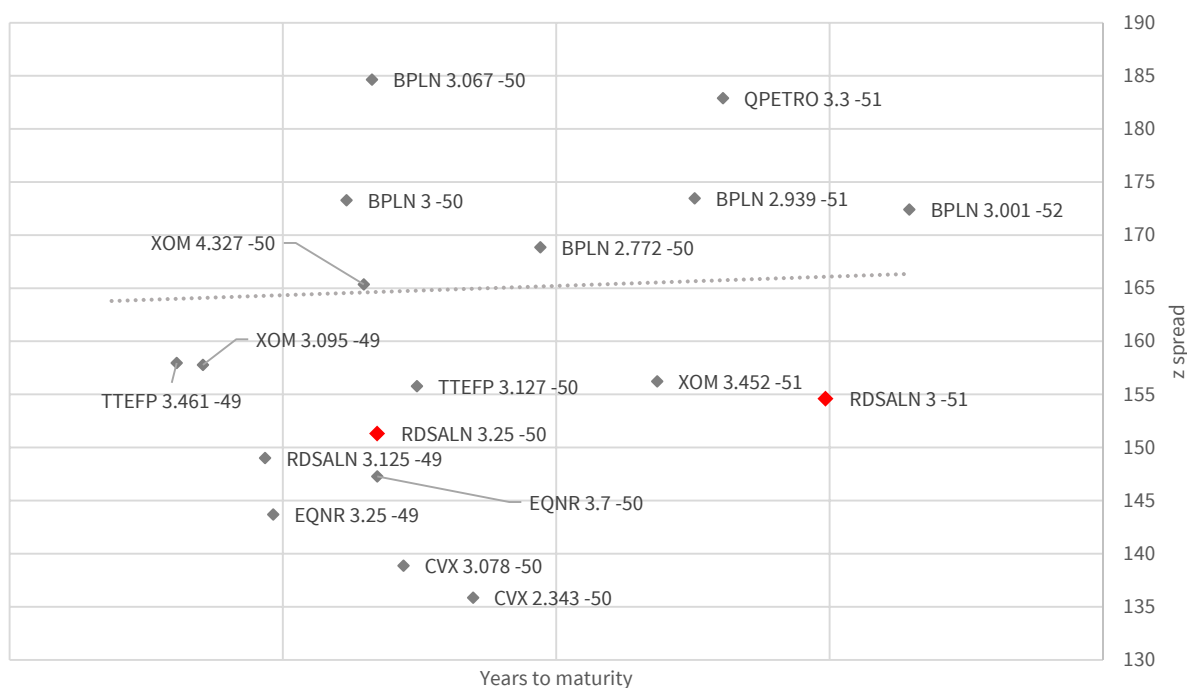
Oil majors in the long end of the USD curve

The RDSALN 3.25 04/50 was issued in April, 2020, just after the valuation trough following the surfacing of the Covid pandemic. On the back of that, it priced just north of equivalent to a z-spread 250bps (CT30+215-220) and obviously had a strong rally in its first year. However, spreads reached a trough in early October and has widened by almost 50bps since then, again see Figure 1.

On Nov 22, 2021, a new 30yr bond (RDSALN 3 11/26 2051, ISIN US822582CL48) was sold and priced.¹⁰ The book was only 2x oversubscribed according to sources, and as Bloomberg expressed it: "[Shell] was able to get its deal across the finish line despite seeing a peak book that was just two times covered" which to us is an indication of a weak book build.

The relative pricing of the old 3.25 2050 and the new 2051 bonds with comps are available in Figure 3. As we can see, the 2051 is now trading slightly wider than the 2050s, in line with the slight upward sloping curve in the very long end. RDSALN trades in the same region as Total (TTEFP) and Exxon (XOM), wider than Equinor (EQNR) and Chevron (CVX) but clearly inside BP (BPLN).

Figure 3. Comps to the old and new 30yr Shell bonds. Source: Bloomberg, AFII.



¹⁰ A smaller USD500mn 20yr 2.875 coupon tranche was also sold (ISIN US822582CK64). This appears to have been a reverse inquiry type of trade, likely as replacement of old 30yr bonds.

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