Early Impacts of Economic Uncertainty for Oil and Gas Companies

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Amid rising economic uncertainty, oil & gas companies are navigating a shifting landscape marked by potential tariffs, commodity price declines, and stock price volatility. While the long-term impact of these forces remains unclear, management teams and compensation committees may be assessing the potential effects of these macro factors on executive compensation and governance programs. In our conversations with clients, two key macro factors are driving potential concerns.

A Moving Target: Tariffs and Their Ripple Effects

While not yet finalized, the specter of tariffs looms large. For oil & gas companies, these tariffs may lead to cost increases and/or supply chain challenges, disrupting near-term planning and adding pressure to both costs and operating margins. Given their unpredictability in timing and scope, tariffs represent a “moving target,” complicating the already challenging task of setting and tracking performance goals for incentive plans.

Volatility in the Markets: Stock Prices and Commodities

Recent commodity and stock price declines and increased volatility present additional headwinds. These fluctuations may distort the projected payouts of in-flight short- and long-term incentive plans, particularly those based on absolute shareholder return. Fortunately, the oil & gas industry has a significant weighting to relative shareholder return in long-term incentive plans which can neutralize for the impact of macro trends. However, short-term market swings, driven more by macroeconomic forces than company-specific performance, could result in temporary misalignment between pay and performance outcomes.

Committee Responses: Flexibility and Focus on the Long Term

As companies take stock of these challenges, compensation committees may wish to understand where they have built flexibility into their incentive frameworks to react to these disruptions. In the near term, we expect a “wait and see” approach to prevail, with few if any changes to in-flight incentive awards. However, committees may consider the broader macro context when assessing performance and making year-end determinations, particularly if tariffs and market volatility have a material impact on performance outcomes.

In the interim, committees may consider the following when evaluating how to respond to the economic uncertainty:

- **Assess the impact of market dynamics** (whether favorable, neutral or unfavorable) to begin to understand the potential impact on in-flight incentive metrics.
- **Confirm the committee’s ability to use discretion** when evaluating incentive outcomes, especially where external factors may materially skew results (likely only applicable to annual incentives).
- **Consider careful sizing of Q2 equity awards** (e.g., independent director or new hire awards), potentially using longer-term average prices or Q1 2025 pricing in lieu of the current stock price.
- **Consider widening performance goal ranges** in the annual incentive plan to absorb some degree of volatility in lieu of adjusting incentive plan targets.
- **Maintain incentives for management teams to proactively manage risks,** so avoid completely neutralizing for unexpected events.
- **Focus on shareholder alignment** and avoid adjustments that fully disconnect pay outcomes from the shareholder experience.

- **Plan for enhanced disclosure** to clearly articulate the rationale for any adjustments, recognizing that such decisions will be scrutinized closely.

Looking Ahead

While it remains too early to predict how the current economic uncertainty will unfold, it would be prudent for boards and management teams to begin to lay the groundwork for a more dynamic and context-sensitive approach to tracking incentive plan payouts and evaluating performance. In the meantime, companies should continue to monitor developments, apply sound governance principles, and maintain a long-term perspective as they navigate this period of disruption.