What Exxon’s deal with Pioneer says about the future of Texas shale

By Amanda Dranep, Staff writers

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A drilling rig operates as the sun sets in Pecos. Its deal with Pioneer Natural Resources would make Exxon the largest operator in the Permian, securing it decades of inventory in a time when the future of the nation’s most prolific oil basin is uncertain.

Jon Shapley/Staff photographer

Oil companies looking for new petroleum-rich plots to tap are hitting a wall in the Permian Basin of West Texas and New Mexico. The desirable “Tier 1” shale that yields ample oil at relatively low cost and minimal technical challenge is largely spoken for.

That’s a challenge for a company with the size and ambition of Exxon Mobil, which plans its growing production decades ahead, and was a key factor in the Spring-based oil giant’s $59.5 billion bid to buy Pioneer Natural Resources. The deal, Exxon CEO Darren Woods said Wednesday, pries open access to “the largest undeveloped Tier 1 inventory in the Midland Basin.”

“They're not thinking about the next two-to-five years, but 10, 20 years,” said Wood Mackenzie shale analyst Ryan Duman, “so, to refill the hopper, so to speak, takes big deals like this. And this firmly moves them into the number one spot with regards to not only Tier 1 inventory, but total inventory.”

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**EXXON GOES BIG:** Exxon expands Texas oil production with $60 billion Pioneer deal

The megadeal, which is expected to close next year, would make Exxon the
largest operator in the Permian, securing it decades of inventory in a time when the future of the nation’s most prolific oil basin is uncertain. Squeezing oil from Permian shale could get harder and more expensive in the years ahead for those who run out of higher-quality source rock.

“I think everybody in the room kind of understands where the Permian sweet spots are,” Ezra Yacob, CEO of Houston-based oil company EOG Resources, said during an investor conference last month, according to a CapitalIQ transcript. “And that rock is getting drilled up.”

The declining availability of quality inventory is drawing lines in the oil patch, separating big players such as Exxon from smaller ones that are seeing a shortening runway, analysts said. This sets the stage for consolidation, as merged companies can more easily weather the higher costs necessary to meet engineering challenges associated with trickier source rock.

While supermajors operating in the Permian Basin have enough quality inventory to last an estimated 25 years at the current pace of drilling, private exploration and production companies would have around 11 years remaining at the current pace, said Matthew Bernstein, a senior shale analyst at Rystad.

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“If these companies start drilling again at 2022’s pace,” Bernstein said, “you’re going to exhaust that inventory in a shorter period of time. For some E&Ps that could be five years or less.”

The moment calls for either a new discovery or new technologies capable of more
efficiently extracting tight oil and reducing the financial burden.

Meantime, the hunt is on for less-desirable Tier 2 shale resources, said Toti Larson, principal investigator at the Bureau of Economic Geology’s Mudrock Systems Research Laboratory at the University of Texas, which specializes in shale research. He said he is seeing growing interest from oil companies in finding what’s left after the prime targets are taken.

This category of source rock tends to be more rich in clay, posing drilling hazards, and rich in natural gas and water, which require additional infrastructure and cost to handle.

“The real question now is how can we continue to make this economic,” Larson said. “You can’t overlook the importance of water disposal and excess gas.”

Still, the basin holds vast amounts of crude waiting to be accessed for those willing to invest the time and money, said Karr Ingham, a petroleum economist for the Texas Alliance of Energy Producers. Plus, he said, a disruptive new technology could always come along.

“I think everybody’s pessimistic about a new technology that’s as revolutionary as the shale revolution,” Ingham said. “But no one expected such a thing to happen in the first place.”

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