Decarbonization & ESG Strategies — An Incremental & Agile Approach

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Introduction and Background

As part of Adamantine's mission to future-proof oil and gas companies against rising social risk, we passionately believe that the game-changing disruptors facing our industry today create the imperative for companies to thoughtfully and strategically articulate their positioning for the energy future. ESG and decarbonization strategies are a key first step in this process and are rapidly becoming a prerequisite for your social license to operate and your ability to continue attracting capital and customers for years to come.

However, we recognize that not all companies are at the same stage in this process. Some are still not convinced ESG should be a priority or are working to understand their drivers and gain the necessary internal buy-in to move forward, while others perceive a sense of urgency but feel they have limited resources for such a large task and have warranted questions around how and where to get started.

At Adamantine, we do not view taking these efforts on as an immediate operational overhaul. Instead, we recommend companies take incremental steps and decisions, yielding a process that is customized towards the appetite and ambitions of your company, but also one that effectively demonstrates your level of dedication, awareness, and progress to your stakeholders.

We have helped a vast variety of clients across the value chain in formulating their ESG and decarbonization strategies and retain years of experience in helping organizations understand and navigate their stakeholder interests and strategic directions. This white paper distills our insights and expertise to provide an overview of Adamantine's approach to ESG and decarbonization strategy development, including key drivers and benefits, available options, and effective ways to get started.

The What — ESG and Decarbonization Strategies Defined

ESG Strategy

At Adamantine, we define an ESG strategy for oil and gas companies as the continuous, company-specific incorporation of ESG risks and opportunities into business operations and decision-making, such that a company is able to proactively narrate its responsible existence and value throughout the energy future. At its core, this process consists of analyzing, addressing, and taking accountability for ESG risks and opportunities.

Of critical importance: A credible ESG strategy must go beyond simply checking a box and describing your activities. Instead, each company's strategy must reflect the meaningful incorporation of ESG criteria into your overall business strategy and clearly articulate your aspirations and planned path forward to improve on them over time. This approach will ultimately require that your company retool its culture, management, and oversight to put ESG-guided priorities at the center of your risk management strategy and execution.

Decarbonization Strategy
We've recently witnessed a multitude of oil and gas companies announcing a rush of net-zero commitments and emission reduction targets. While it may be easy to dismiss "decarbonization" as a buzzword, that would be a mistake. In reality, decarbonization targets are a meaningful component of business strategy for oil and gas companies of all sizes and sectors. A decarbonization strategy both supports your ESG strategy and also should be informed by what you learn from developing your ESG strategy.

Every company can and should narrate its place in the decarbonized energy future that the public expects. A properly developed decarbonization strategy allows you to clearly articulate the steps you are taking to reduce emissions and how your business is aligned with this collective goal.

The Why — Key Drivers and Benefits

For companies that are still working to frame their drivers, navigate reluctance, and gain the requisite internal buy-in to get started on ESG and decarbonization strategies, it is important to understand the multifaceted pressures the industry faces and how both strategies can give your firm a competitive advantage with access to a range of material benefits. Below we have outlined some key drivers and benefits of these strategies.

ESG Strategy — Drivers and Benefits

Game-changing oil and gas leaders know that ESG:

- **Matters to private equity, too.** A 2020 survey of leading private equity firms found 93% believe a focus on ESG will generate good investment opportunities.
- **Increases your access to capital.** ESG is about showing your company's ability to achieve sustainable, long-term growth — which in turn attracts investors and capital. Investors are under their own pressure to seek sustainable investments.
- **Enhances your reputation.** Looking for an eventual exit? ESG topics can directly impact your reputation with stakeholders and therefore the reputational risk for potential transaction partners. In another company's due diligence, what will your stakeholders say about you?
- **Helps you benchmark proactively.** It might be scary to understand how your ESG metrics compare to your peers, but it will position you in a proactive (rather than reactive) stance.

Decarbonization Strategy — Drivers and Benefits

Game-changing oil and gas leaders know that on the topic of decarbonization, there are many applicable drivers and benefits:

- **Climate goals are real and depend on us.** Global, federal, and state leaders have climate-related goals which cannot be reached without us. According to McKinsey, the oil and gas industry accounts for 9% of all human-made greenhouse gas emissions and produces the fuels that create another 33% of global emissions. By working proactively *with* game-changing leaders like you, policy leaders can accelerate results while allowing business flexibility in solutions.

- **Investors are paying attention.** As recently as April, BlackRock doubled down on its request to portfolio companies to align their business with a net-zero future. Your investors are undoubtedly paying attention.
- **Carbon could cost you.** Although the timeline and likelihood of carbon pricing is unclear, we know it is on the table. Getting a handle on your present and future carbon footprint now is a must.
- **The public wants it.** Polling continues to show that the public believes climate change is an issue that needs to be addressed. This is the stakeholder environment in which your company operates.
- **Regulations will come.** Federal air regulations are looming, and more states are exploring stringent regulations around air quality. A proactive stance regarding your emissions footprint will better position your company to negotiate regulatory flexibility.

The How — Your Options

There are many ways game-changing leaders can show progress and intention to investors and stakeholders on ESG and decarbonization. In line with our incremental approach, here are some small yet impactful steps we typically suggest to set your company up for success.

ESG Strategy Options

- **Build an internal team.** Any successful project involves accountability. ESG requires input from a cross-section of departments within companies. Launch a team of high performers representing your core departments. Charge them with developing your ESG strategy and empower them to bring in leadership at key junctures.
- **Assess your risk.** Analyze your risks to reveal your drivers for an ESG strategy, your bespoke priorities, and the optimal timeframe to address or prepare. Consider the following drivers:
    - Expectations of your investors (one common example: publicly disclosing emission metrics by a certain date);
    - Potential regulatory and policy developments in your region (e.g., imminent flaring regulations);
    - Shifting demographics (such as the rise of the millennials);
    - Peer commitments and initiatives (e.g., methane intensity reduction goals);
    - Risks to employee retention (such as local peers embracing DEI); and
    - Community interests (one common example: water use concerns).
- **Gather metrics.** Investors want transparency around your operations. Start by gathering the metrics you already measure and see how they compare to those of your peers. Some examples include freshwater use, Scope 1 emissions, Total Recordable Incident Rate, and employee diversity. This will help you understand where you need to improve and what you can highlight. From there, consider new metrics by analyzing peer reports and respected global reporting frameworks from the Sustainability Accounting Standards Board (SASB) and Global Reporting Initiative (GRI).
- **Consider a report.** Companies hesitate to develop external reports because they assume they have to be deeply comprehensive and utilize global reporting frameworks. There

are a range of acceptable efforts as long as you have a public plan to improve over time. Consider starting small and building up:

    - Community Impacts Report: Focus on community impacts such as employee volunteering, community investment, and best management practices used to mitigate impacts to the community. This focus helps you understand the report-building process, provides collateral for stakeholder discussions, and improves transparency.
    - Corporate Social Responsibility Report: Focus on responsible operations and company practices by disclosing metrics that show you are considering your impacts to stakeholders including employees and the broader community.
    - ESG or Sustainability Report: Use frameworks like SASB and GRI to ensure you are disclosing the metrics that matter most to investors. This type of report will include analysis of company systems to manage impacts and ESG topics.
- **Consider targets:** Some investors and environmental groups argue "the meat" of an ESG strategy consists of public targets and commitments to improve ESG metrics.
    - Consider any targets you could make related to meaningful ESG topics and whether they can be tied to executive compensation.
    - Want to make a meaningful commitment? Consider a commitment to end routine flaring by a specified date.
    - When evaluating an emission-related target or commitment, consider working toward calculating emissions using measurement rather than estimation.
    - Think about how you can show investors and stakeholders that you are willing to go above and beyond both current and expected regulatory requirements.
- **Set a 3-year strategy:** Develop a flexible strategy that allows course corrections and key milestones to keep you on track. When will you have metrics gathered? When will you release your first report? Being able to articulate your path will be helpful in external discussions.

Decarbonization Strategy Options

- **Reduce your emissions.** Despite the many pathways to the energy transition, *every pathway* requires solving Scope 1 emissions and demonstrating quantitative improvement. Consider this a priority, make a plan you are accountable to, and act on the low-hanging fruit now.
- **Constructively engage.** Industry trade associations often play important roles — but they are too often pushing back on decarbonization rather than co-creating impactful outcomes that build toward a shared energy future. Game-changing leaders will not be afraid to break out from the pack. Take opportunities to constructively engage with policy makers, investors, stakeholders, and eNGOS directly. There are infinite opportunities to innovate solutions and find bespoke technological practices that can work for your business, operating community, and stakeholders.
- **Build your decarbonization toolbox.** Your company's decarbonization toolbox can start small and evolve over time. It can include items such as emissions reductions, R&D partnerships, and participation in demonstration projects. Build a strategy with a range of options for different timeframes and resources to allow your team flexibility. If

resources are limited, narrow your focus to monitoring and mitigating methane for the most impact. Many trades have committees sharing best practices on emissions reduction. There's no shortage of external guidance; for example, check out the Methane Guiding Principles' *Best Practice Toolkit*.
- **Explore low-carbon energy integration.** Electrification of operations with renewables or fuel-switching drilling operations to natural gas and other low-carbon energy sources can support operations. Have a working group explore your options. Important: Consider this *after* you have addressed your own emissions. Slapping solar panels on your site won't fix the problem or convince anyone that you are taking the issue seriously.
- **Make a commitment.** It will be important for companies of all sizes to start making both aspirational and specific emissions reductions commitments. Aspirational commitments are directional in nature and demonstrate both your interest and willingness to work on decarbonization. Emissions reductions should be specific and actionable. Ultimately, pledges will only get a company so far. Within a year, companies should be able to demonstrate investments in aspirational goals and quantifiable emissions reductions. Support any emission reduction commitments with capital allocation and near-term milestones to ensure action.
- **Find partners.** Decarbonization is a busy space! Seek partnerships or projects with other parts of the value chain, investors, startups, community organizations, academics, and environmental groups. There is a wealth of coalitions helping companies innovate and navigate decarbonization.

Getting Started

ESG First Steps

- **Talk to your investors.** Understanding your investors' priorities and expectations can avoid unnecessary work and resource depletion. Investors appreciate a proactive stance and an open dialogue. Bringing up ESG won't change their course and increase their expectations; it's already on their minds!
- **Hold a strategy session to assess your risk.** Bring together your team or working group to brainstorm risks and opportunities. Provide them prompts beforehand and charge them with bringing their best ideas. Need buy-in? Have leadership frame the effort as a priority.
- **Get a handle on your emissions.** For the oil and gas industry, methane emissions are a top indicator of sustainability. Understand how your emissions stand up to those of your peers as well as public commitments made by larger companies. Determine how you can get closer to reporting actuals versus estimates.

Decarbonization First Steps

- **Get a handle on your emissions.** Taking a deeper dive from what you learn in developing an ESG strategy, get started today on understanding your emissions. This doesn't require perfect data to get started as long as you commit to continuous improvement in your data collection and analysis. Estimation will suffice for a time,

and then measurement will be the long-term goal. Start by striving for more transparency through high-quality data. Answer these questions:
    - What steps are we taking to understand our methane emissions?
    - What have we learned so far about the most significant sources and causes of emissions in our systems?
    - What actions are we taking to continue improving our understanding and reducing our emissions?
- **Start with flaring.** More and more companies are making flaring reduction a priority. Consider a flaring reduction target that is quantitative and time-bound. Consider governance incentives and midstream collaboration to set and meet targets.
- **Talk to your investors.** As with ESG, understanding your investors' priorities and expectations can avoid unnecessary work and resource depletion. In addition, when a smaller company approaches their investors, they often find there are other companies in their portfolio facing the same issues. The investor can bring companies together to share best practices and collaborate on decarbonization solutions.
- **Talk to your stakeholders.** Regulators, employees, and community leaders can help you think of creative solutions that suit your company's specific footprint.
- **Allocate resources.** You will have to shift resources to decarbonization to make progress — whether that's putting them towards building a decarbonization working group; creating and growing an innovation team (like many of our game-changing clients); funding new infrastructure; or investing in innovation.

Conclusion

Given the game-changing disruptors facing our industry today, Adamantine strongly recommends your company thoughtfully and strategically articulate its positioning for the energy future. Developing ESG and decarbonization strategies are a key first step in this process. They are rapidly becoming a prerequisite for your social license to operate and your ability to continue attracting capital and customers for years to come.

While there is no one-size-fits all approach, any player — no matter their size — can develop these strategies by taking incremental and structured steps. Taking the time to proactively formulate and internalize your path will allow you to align stakeholders, embrace disruption, and open the doors for your company to seize the moment and thrive.

Remember, ESG and decarbonization strategies should account for your company's unique position, inform your overall business strategy, and result in meaningful action. Combined, they will position your company to navigate our evolving operating environment while creating enduring value for all stakeholders.

Seize the Day

Above, we have provided our framework and key suggestions you can use to start moving the needle. If you are looking for additional resources as you embark on this journey, Adamantine is ready to support your ESG Strategy. Contact us today for a discovery call.