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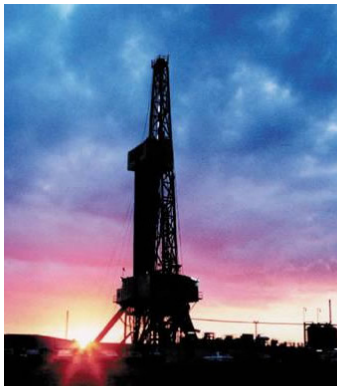
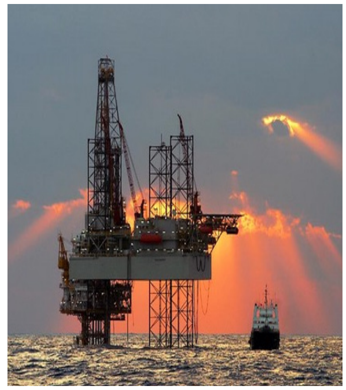


November 2012

Innovation Unnoticed:

Moving the Needle on Energy Public Relations

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To Our Clients and Friends:

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From time to time, Perry Street Communications offers commentary and perspective on financial and corporate communication matters. We have traditionally done so in response to current events (proxy battles, the financial crisis, and the Toyota recall, to name a few), but in this instance were inspired to take a broader look at the energy industry which, despite well-funded and spirited public outreach campaigns, cannot shake the vestiges of lingering, often negative, public perception.

In this memorandum, Perry Street assesses the state of play for the energy industry in this regard, examines what's worked and what has not, and provides a roadmap for the future. The findings are not intended to provide definitive answers, but rather to anticipate areas of improvement and provoke thought.

We hope you benefit from the research and perspective.

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Introduction

In the world of our fathers, oil industry executives operated in small but influential circles where personal relationships, often cultivated outside the glare of public view, were the foundation upon which many an empire was built.

Those days are long gone, of course, replaced by the often frenetic digital community that has transformed business and political cultures across the globe. With its insistence on transparency, access and immediate accountability, CEOs and world leaders ignore these dynamics at their own peril.

The energy industry has responded accordingly, investing millions of dollars in the public engagement process. *Yet time and again, we see that the substantial transformation within the oil sector has not been fast enough to fend off smaller foes which successfully utilize digital technologies as a viral organizing tool.*

Even high-stakes political showdowns – such as consideration of the Keystone XL Pipeline deal – have failed to produce the decisive victories the industry's muscle once commanded.

In "Keystone: How the Oil Industry Brought a Knife to a Gunfight,'' *Forbes* recounted how the energy industry was outmaneuvered on Capitol Hill, not by elected officials, but by public interest groups using little more than Facebook and Twitter accounts.

"As we conducted our research into the state of the energy industry's corporate engagement practices, we readily found reputation-busters across the media spectrum."

"Suddenly we see that a well-integrated grassroots initiative driven by superior digital strategies can trump the conventional inside-the-Beltway politicking of even so formidable a presence as the oil industry,'' *Forbes* concluded.

Importantly, the political challenges have come despite the industry's substantial efforts to actively manage its reputation. Oil companies, both individually and as a group, have showcased their positive impact on job growth and energy independence. They've made concrete, specific inroads addressing environmental and safety concerns, as well as relating the industry's day-to-day work to everyday concerns: jobs, manufacturing and energy independence.

And, yet, a reality check is in order: despite these efforts – and untold millions of dollars in public awareness, marketing, and advertising campaigns – positive developments in the energy sector are frequently overshadowed by the sheer number of legacy, negative stereotypes coming not only from the sector's political and cultural foes, but from a broad array of self-appointed experts who shape public opinion through a variety of media platforms.

As we conducted our research into the state of the energy industry's corporate engagement practices, we readily found reputation-busters across the media spectrum:

- The 1980's TV show Dallas recently found a second life in the popular "reboot,'' providing new spin on old myths about cartoonish oil barons.

- "Private Empire: Exxon Mobil and American Power,'' which was published to critical acclaim earlier this year, is a 685-page tome that one reviewer said "opens with the Exxon Valdez oil spill in Alaska in 1989 (the captain had been drinking), and closes with the BP Deepwater Horizon nightmare in the Gulf of Mexico in 2010. In between there is much for those who loathe Big Oil generally, and Exxon Mobil specifically, to feast upon.''

- The potential good news about a University of Texas fracking study turned into a major unforced error and public relations nightmare this summer when critics learned that the author, UT professor Charles Groat, failed to disclose his own financial ties to the oil and gas industry. Instead of easing public concerns about hydraulic fracturing with persuasive science, the study generated international headlines that raised questions, fairly or not, about the author's integrity.

Against this backdrop, it's almost impossible to plausibly suggest that the industry's efforts to soften its image have produced the desired results.

So we spent some time asking a few questions that seem distinctly relevant today – at a time when the industry has a unique opportunity (as we detail later in this paper) to capture the public imagination as never before:

- What are the key drivers of change that, factually, *should* be supporting a public relations renaissance for the industry?

- Why, despite these changes, does a stubborn "perception gap" still exist with the public?

- What can the energy industry learn from its non-energy peers?

- What are the lessons learned concerning such efforts: what's working, what isn't, and where is there room for improvement?

These questions, in turn, are intended to address a larger one: *Why, of all the major industries, is energy the one that has the most difficulty moving the needle on public opinion?*

As one might expect, the answers to these questions are far from scientifically-derived. Rather, our goal in compiling this paper was to sift through media coverage, industry dynamics, and energy companies' existing communications efforts looking for practical ideas that energy companies of all sizes can consider as they turn to 2013 and beyond.

Pop Culture, Business Reporting and Energy: An Uneasy, Evolving Alliance

Thirty years ago, the *Wall Street Journal* covered the energy sector and *Rolling Stone* covered the music scene. Today, *Rolling Stone* is still covering Led Zeppelin and Bob Dylan - along with a widely-read profile of Chesapeake Energy's CEO Aubrey McClendon that had a profound impact on perception of the industry.

When *Rolling Stone's* Jeff Goodell committed to writing an article about Chesapeake's fracking business and tremendous growth in its March 15, 2012 issue, the Company made a strategic (and, no doubt, well-intentioned) decision to allow the reporter seemingly unfettered access to McClendon. McClendon and Goodell at dinner. McClendon and Goodell waxing nostalgic about Chesapeake's formative years. McClendon and Goodell drinking wine.

The result? A disaster. The story, "The Big Fracking Bubble: The Scam Behind the Gas Boom," constituted a brutal takedown of Chesapeake, and was an embarrassment for McClendon personally and professionally. Chesapeake's VP of communications subsequently explained what had happened in an open letter to employees:

> When we were first contacted by *Rolling Stone* and looked at the writer's prior work, blog posts, and tweets, we figured we'd never get a fair shake and suggested he talk to other industry groups to get a perspective on natural gas. But when he declared his intention to write a story focused on our company and Aubrey – with or without our cooperation – we decided that providing the full transparency that the media and our critics so often demand from our industry would potentially result in a more honest and fact-based story. Although our expectations for honesty and fairness were quite low, the writer failed to reach even that low bar.

This is a classic case of good intentions failing to align with effective execution. While Chesapeake deserves credit for providing transparency, it should have been quite obvious that Goodell's prior, highly-critical writing – along with *Rolling Stone*'s harsh assessment of Goldman Sachs and other business giants – made a fair shake virtually impossible.

Chesapeake's public relations strategy ran headfirst into the buzzsaw of business reporting as an extension of pop culture reporting – with all the hyperbole, hyperventilation, and drama such a dynamic suggests. This trend started with *CNBC*, and the scandals and governance crises of the past 10 years have added fuel to the fire. As a general matter – whether it's an environmental, financial, or other threat – business reporters are loathe to "miss" a big story, as highlighted by Columbia Business School: "The mortgage crisis, which is costing millions their homes and has driven the world to the brink of an economic abyss, has raised difficult questions for the nation's business press. Why was the public taken by surprise? What kind of reporting was missing and what kind is needed now? What are the lessons for financial journalism and what is its true purpose."

"We suspect that part of the problem stems from the industry's own internal ambivalence about embracing its status as a retail/ consumer-facing operation."

The bottom line: a chastened business press plies its trade in a cultural environment where business scandal is tantamount to pop culture scandal. Decisions about how, when, and where to cooperate with the media must be made accordingly and with vigilance.

This is not to suggest that many in the energy industry haven't internalized this fact, and yet when some of the largest players continue to commit unforced errors, the discussion merits further investigation. We suspect that part of the problem stems from the industry's own internal ambivalence about embracing its status as a retail / consumer-facing operation.

The Retail Dilemma

Traditionally, the energy sector simply has not viewed itself as a consumer-facing industry. The mentality of a wholesale producer took hold at an early stage in the industry's formation, and vestiges of that mindset remain to this day. As John Hofmeister, former President of Shell Oil Company, puts it, "By the time a tanker's load of gasoline is delivered to the retail station, the oil executive has moved on to think about the gasoline that will be delivered 10 to 25 years in the future.''

The net result, unfortunately, is that consumers and CEOs are at arm's distance from each other. In cases such as this, unfamiliarity breeds contempt. One poll released recently by The University of Texas at Austin found less than 14 percent of Americans think the country is headed in the right direction on energy.

Even assuming there is a natural, "baked-in" opposition to the industry as a whole from environmental groups and those similarly aligned, a 14 percent consensus speaks to an industry that, despite investments in blogs, Twitter handles, and retail-oriented advertising, it is not connecting on the retail level.

But why?

The answer, we believe, is <u>not</u> that the industry has failed to recognize the need to connect with consumers or failed to incorporate engagement efforts into its mission.

The problem, quite simply, is that engagement efforts have been executed with a mindset that – at its core – remains commercially focused. Energy companies are adopting many of the tactics that fuel retail engagement, but are missing the nuance that has the potential to move the needle.

Consider Goldman Sachs as a company that appears to have successfully made the transition from commercially-minded to much more retail-oriented. A few facts for context:

• The Firm is *perceived* to have played a central role in the recent financial crisis. There has been no shortage of public scorn directed to its executives, its deal-making, its alleged marketing of financial products that were 'designed to fail,' and the abundant presence of Goldman alumnae at the highest levels of Washington policy-makers.

• *Rolling Stone* (them again) famously referred to Goldman as a "…great vampire squid wrapped around the face of humanity, relentlessly jamming its blood funnel into anything that smells like money."

• In March 2012, a Goldman Sachs Director, Greg Smith, resigned via an op-ed in *The New York Times,* in which he claimed (among other allegations) that, "…the interests of the client continue to be sidelined in the way the firm operates and thinks about making money."

• Allegations of insider trading by a former Board Member, Rajat Gupta, hounded the Company for months.

In response to these (and other, related challenges), Goldman first adopted a public relations strategy that should sound very familiar to the energy industry: correcting and rebutting false information.

Beginning about a year ago, however, Goldman shifted course to a more proactive approach that emphasized transparency, humility and – frankly – the need to change the minds at a retail level. Example: Goldman partnered with Warren Buffett (is there any better embodiment of retail affiliation?) to launch a Goldman-sponsored and funded, "10,000 Small Businesses Initiative." This platform enabled Goldman (and Lloyd Blankfein) the opportunity to reframe the Company's relationship with the American economy as one that supports entrepreneurs at the retail, man-on-the-street level. It also provided abundantly positive public relations opportunities: Buffett and Blankfein on *CNBC*, speaking platforms, an impressive microsite, and events around the country.

Lloyd Blankfein has also sharpened his retail message by embracing a topic that is both newsworthy, and has absolutely nothing to do with Goldman's underlying work. Specifically, he has emerged as a vocal supporter of gay marriage – a platform that accomplishes several goals: (1) it puts him on common ground on an issue that many of Goldman's critics on the left also agree with; (2) it fuels the perception of Goldman as a place that is willing to "stand for something" other than making a buck; (3) it reinforces the notion that Wall Street stands for an egalitarian, merit-based culture.

Agree with his stance or not, many of Goldman's critics have been de-fanged by his embrace of the issue. Goldman has taken many, smaller steps to engage the retail audience: a YouTube channel featuring employees talking about the Company and its good deeds, and removal of proposals from its proxy that would have otherwise been construed as shareholder-unfriendly, among other initiatives.

The point is this: from where we sit, the energy industry remains largely absorbed in the first step of the Goldman public relations initiative described above: justifying its existence, rebutting critics, educating audiences. This is important, to be sure, but it isn't enough. The industry needs to adopt a sense of urgency to move to the next level of retail engagement. Rather than being delegated down the corporate food chain, engagement efforts should be embraced at top levels by CEOs as a vital function of a winning business plan. Take a unique stand on an issue that has absolutely nothing to do with energy. Ramp-up efforts to add dimension to how Senior Management is perceived by the public at large. Disarm and surprise critics to the upside; **BE BOLD.**

Real Benefits

For a moment, we will channel what we expect would be the reaction of many energy industry executives to these recommendations: why does any of this matter? *Our enterprise value reflects the underlying business, fundamentals are strong.* What do we have to gain?

"...engagement efforts have been executed with a mindset that – at its core – remains commercially focused."

The short answer is that reputation and public perception are hard-wired into enterprise value as never before. Significantly, much of the research shows that corporate success is defined not only by what's produced from a promising well or new gas field discovery. It is also inextricably tied to engagement with the public, corporate reputation, and solid corporate citizenship.

Hard data shows that a coordinated communication effort:

- Translates into real value by making your stakeholders more likely to engage in behaviors that boost your bottom line.
- Makes consumers more likely to buy the company's products or services and recommend them to others.
- Prompts talented employees to join the organization, stay with the firm, and give their best effort.
- Contributes to a strong market valuation and attracts investors.
- Serves as a reservoir of good will, making it easier for customers, media, and other stakeholders to give the firm the benefit of the doubt in times of crisis.
- Advances a responsible regulatory and legislative agenda that in turn creates a more favorable business environment and allows companies to do things needed to be profitable.

These findings are undisputed and underscore the need for the industry to become far more aggressive and strategic in managing its reputation campaigns and, as discussed above, retail consumers, with their long list of concerns ranging from gas prices to climate change.

As summarized by the advertising firm, Ogilvy & Mather:

> Business has become more fluid and transparent since the Internet liberated information and lubricated communication. It's easier than ever for people to decide whether they approve of businesses and institutions and to share those feelings with other interested parties. Audiences cannot be neatly segmented and isolated, with this one knowing that and that one knowing this. For companies with appealing philosophies and beliefs, this creates great opportunity. Those with something to hide see this as a threat. [1]

Indeed, *The Economist Intelligence Unit* has found that 75 percent of a company's value (regardless of its size) is tied up in its reputation. There is no "size" bias here; smaller energy firms' misdeeds can have a detrimental impact that far exceeds its market cap – particularly with many such companies aggressively pursuing exploration and development opportunities around the globe. Another study by the Reputation Institute found that 57 percent of the public's willingness to say something positive about a company is driven by how they perceive the corporation's values and behaviors, while only 43 percent is driven by what they think of the company's products and services.

For companies navigating this new reality, it's akin to playing three-dimensional chess: fundamentally transforming corporate communications and public engagement strategies while the very tools of communication (the internet, social media, democratization of information in general), are changing just as quickly.

The good news is that the industry's underlying fundamentals are strong, and should provide a solid platform for a more proactive, confident, retail-oriented approach. Three major points underscore this reality:

Energy Independence: From the backyards of Ft. Worth to the Canadian sands to the deep-water Gulf, new technologies are leading to a renaissance in conventional fuels. As Ivan Sandrea, president of the Energy Intelligence Group, stated, "The fossil fuel age will be extended for decades …. Unconventional oil and gas are at the beginning of a technological cycle that can last 60 years. They are really in their infancy." A dozen years ago, shale gas amounted to only about 2 percent

1"What's the Big IdeaL," by Colin Mitchell and John Shaw, Ogilvy & Mather of United States production. Today, it is 37 percent and rising. A team of analysts and economists at Citigroup has even argued that the U.S., or at least North America, can achieve energy independence by 2020, as more domestic production and doubling down on conservation produce a virtuous cycle. Even nuclear is in the mix, with deep-pocketed investors like Bill Gates leading the charge on making smaller, cheaper, and safer nuclear reactors. [1]

Conservation: Over the last 20 years, the U.S. has made enormous and impactful strides in energy conservation efforts. According to McKinsey, since 1980, energy consumption per unit of floor space has decreased 11 percent in residential and 21 percent in commercial sectors, while industrial consumption for real dollar of GDP has decreased a dramatic 41 percent. McKinsey further estimates gross energy savings of $1.2 trillion if truly holistic and scaled energy conservation measures can be adopted and successfully implemented – a big "if," to be sure, but the potential is there.

Energy sector as engine of economic growth: Even as the overall economy remains sluggish, the positive contributions from the energy sector are undeniable. The jobs report from March 2012, for example, showed that employment in oil and natural gas extraction grew by 3,100 – nearly twice as much as the previous month. Over the past year, the "oil and gas extraction" category has added 26,300 direct jobs – an increase of 16 percent, compared to 1.5 percent growth nationwide. As *The Wall Street Journal*[2] reported, the boom in energy production in the United States gives a distinct competitive edge to U.S. producers of fabricated steel, transportation equipment, machinery and chemicals, which use natural gas extensively – a key contributor to America's "Manufacturing Renaissance," according to Neil Dutta, U.S. economist at Bank of America Merrill Lynch.

The net impact of these changes is a tectonic shift in the energy landscape compared to just a few years ago. The notion of U.S. energy independence is no longer laughable. As Daniel Yergin, chairman of IHS Cambridge Energy Research Associates recently wrote, the impact is being articulated at the highest levels:

"This is a solid, enviable base upon which to move forward with the 'next phase' of the energy industry's public engagement efforts."

> The impact is becoming evident in the way America talks about energy. President Obama's address to Congress in February 2009 was all about "clean, renewable energy" and called for doubling "this nation's supply of renewable energy in the next three years." His 2010 State of the Union address was about "clean energy jobs." He had barely a word for oil and natural gas in those speeches. In his 2012 address, the president caught up with the new reality and spoke with quite a different emphasis. "This country," he declared, "needs an all-out, all-of-the-above strategy that develops every available source of energy." He pointed to the near-doubling of renewable energy use since 2008 and rightly emphasized their importance to the nation's future energy mix. But this year he devoted almost as much time to natural gas and oil as to renewables. His announcement that "American oil production is the highest it has been in eight years" turned out to be an applause line. [3]

Thus, in a very short period of time, the energy industry has been largely transformed. What was once viewed as a slow-moving, sclerotic industry is now driving innovation, jobs, and positive change as never before. And it has been technology, Americans' favorite innovative force, which has largely driven the transformation.

"The energy industry may well be the highest tech industry in the world," says Joe Stanislaw, a senior advisor on energy and sustainability for Deloitte. "When you're drilling down two, three, four, five miles, that's like going to the moon."

The industry is creating jobs, adding to a brighter future for manufacturing and more responsive to environmental concerns than ever. **This is a solid, enviable base upon which to move forward with the "next phase" of the energy industry's public engagement efforts.**

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1 "U.S. energy independence is no longer just a pipe dream," by Tim Mullaney, USA Today, 5/15/2012
2 "The Great Reversal: Playing the U.S. Manufacturing Boom," by Jack Hough, The Wall Street Journal, 4/6/12.
3 "America's New Energy Reality," by Daniel Yergin, The New York Times, 6/9/12.

The Way Forward

Having articulated the state of affairs, the challenges, and the case for a more optimistic future, the logical question for any energy Company is: what do we do? Certainly, there is no one-size-fits all prescription, but there are some governing principles with broad applicability:

• **Don't Confuse Strategy with Tactics:** From sustainability campaigns to Twitter handles to blogs, there is abundant evidence that energy companies "get it," in the sense that they understand the power of communication and have invested in tools accordingly. But these are merely means to an end – new, exciting tactics – that should not be confused with cohesive and thoughtful messaging and engagement that anticipates risk while fostering durable relationships with stakeholders.

• **CEO - Front and Center:** No longer a resource to be deployed only sporadically, leading CEOs in the industry must ramp up public engagement (note that this does not include granting full access to a *Rolling Stone* reporter). The public expects no less, and in a vacuum the voices of critics only grow louder and more prominent. Communications planning and execution at the highest management levels of the organization must be managed like any other irreplaceable corporate asset. Example: when Apple confronted allegations of worker mistreatment at the Foxconn assembly plant in China, CEO Tim Cook embarked on a widely-lauded tour of the factory, allowed the Fair Labor Association to begin inspections, and subsequently spent the first nine minutes of an investor presentation discussing the topic, touching on problems in the supply chain and new initiatives the company has put in place to assure those problems do not happen again.

"Part of the evolution towards a retail mentality involves a serious re-think of the tone with which much of the industry communicates."

• **Change the Subject....Disarm the Critics:** In many cases, it seems that even when the largest energy companies try to change the subject or invest in a worthy cause, there remains an implicit connection to underlying business goals. This only fuels the cynical perception that, at the end of the day, it's ultimately about the bottom line. We advocate for thinking outside the box to engage a topic completely unrelated to energy that causes a paradigm shift in perception. The specific issue is less important than the conviction.

• **Tone Matters!:** Part of the evolution towards a retail mentality involves a serious re-think of the tone with which much of the industry communicates. In short, it is often defensive, bordering on frustrated, concerning the public's inability / unwillingness to learn the true facts. This is not the foundation upon which a relationship of trust and respect is nurtured, and with abundant evidence that we are in the midst of an energy renaissance, the tone should be no different than that of Jack Welch, Henry Ford, Steve Jobs or others like them: relentless optimism, candor, and an outward display of energy that is infectious. After all, industry dynamics support these characteristics – why shouldn't management's demeanor do the same?

• **Emotional Intelligence:** In the realm of public relations, the energy industry heavily emphasizes structured, rational arguments, and data – an almost clinical approach that seeks to systematically reframe issues, educate the uninitiated, and arm supporters with facts. This is important, to be sure, but it will never move the needle in any appreciable manner;

> Business should by now understand that successful companies are those which are outward-facing and which understand not only who their audiences are, but also what they think and what they want. So why are companies so often surprised by controversy? Probably because they are used to rational decision making based on technical and scientific data. They fail to understand that an issue can be viewed in many different ways and that emotion is a powerful change-maker (emphasis added). [1]

The energy sector would be well-served, we believe, by internalizing the power to shift perception through emotion that goes beyond traditional advertising. Consider Blankfein on *CNBC* with the young entrepreneur, Cook at the Foxconn factory meeting workers, Starbucks' Howard Schultz investing his brand and reputation on a "Create Jobs for USA" Initiative – all are evidence of strong emotional intelligence at the CEO level that accrued to the Company's benefit.

1 Shige Makino and Tome Roehl, "Learning from Japan: A Commentary," Academy of Management Perspectives 24, no. 4 (2010) 40.

Going Forward

Myriad factors point to an immensely bright future for the energy industry – the opportunity is there to capture this moment and transform public perception. Doing so does not require a radical departure from the meaningful investments in public relations and communications over the last several years. Rather, the goal is to urge the industry as a whole to assess what's worked, what has not, and adopt complementary strategies that are responsive to today's complex landscape.