



Imperial Oil (IMO)

Updated November 8th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	\$32	5 Year CAGR Estimate:	11.2%	Volatility Percentile:	43.0%
Fair Value Price:	\$27	5 Year Growth Estimate:	13.0 %	Momentum Percentile:	38.8%
% Fair Value:	120%	5 Year Valuation Multiple Estimate:	-3.6%	Growth Percentile:	97.1%
Dividend Yield:	1.8%	5 Year Price Target	\$49	Valuation Percentile:	29.4%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	73.1%

Overview & Current Events

Imperial Oil is one of Canada's largest integrated oil businesses. The company operates through three reporting segments: Upstream, Downstream, and Chemical. Imperial Oil is headquartered in Calgary, Alberta, Canada. Exxon Mobil (XOM) owns approximately 70% of Imperial Oil's common equity. Imperial Oil is cross-listed on both the Toronto Stock Exchange and the New York Stock Exchange, where it trades with a market capitalization of US\$25 billion. Imperial Oil reports financial results in Canadian dollars, but the figures shown in the data tables of this research report have been converted to U.S. dollars and refer to the company's NYSE-listed shares.

Imperial Oil is completely different from the well-known integrated oil majors, such as Exxon Mobil and Chevron, in one aspect. While the well-known oil majors generate most of their earnings from their upstream segment, Imperial Oil generates most of its earnings from its downstream segment. In the first nine months of the year, Imperial Oil has generated 76% of its earnings from its downstream segment. The reason is that its refineries enjoy markedly high margins thanks to the use of heavy Canadian crude as input. This type of crude trades at a deep discount to WTI, which in turn trades at a wide discount to Brent. This competitive advantage of Imperial Oil is paramount.

In early November, Imperial Oil reported (11/2/18) its financial results for the third quarter of fiscal 2018. Its earnings essentially doubled while its earnings-per-share jumped 114%, assisted by share repurchases. The upstream segment more than tripled its earnings, from CAD\$62 million to CAD\$222 million, mostly thanks to the rally of the oil price since last year. More importantly, the downstream segment increased its earnings by 72%, from CAD\$292 million to CAD\$502 million, thanks to strong refining margins, which resulted from the discount of Western Canadian Select (WCS) to WTI, which widened from \$10 per barrel in Q3-2017 to \$22 per barrel in Q3-2018.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$3.58	\$1.76	\$2.48	\$3.77	\$4.35	\$2.98	\$3.30	\$1.17	\$0.56	\$0.86	\$1.90	\$3.50
DPS	\$0.31	\$0.35	\$0.40	\$0.44	\$0.48	\$0.46	\$0.45	\$0.39	\$0.44	\$0.50	\$0.58	\$0.75
Shares	859.40	847.60	847.60	847.60	847.60	847.60	847.60	847.60	847.60	831.24	800.0	750.0

Imperial Oil's earnings-per-share history has been volatile, largely due to the high volatility of refining margins and the downturn in oil prices that began in 2014. Indeed, 2017 earnings-per-share were less than one-fourth of their peak levels. With that said, Imperial Oil has earned \$1.38 per share in the first nine months of the year. While the fourth quarter is generally weak for the refining segment, it will benefit from reduced downtime in some facilities of the company compared to the last two quarters. Therefore, we expect earnings-per-share of around \$1.90 for this year, with continued growth to \$3.50 in 2023.

There are a number of factors that lead us to believe that continued growth is possible for Imperial Oil. According to the company's estimates, Canada has the third-highest level of oil reserves worldwide, behind only Venezuela and Saudi Arabia. Imperial Oil expects to grow its production by 15% from 2018 to 2020. Opportunistic share repurchases should also play a role in Imperial Oil's per-share growth. The company's share count has decreased by 5% in the last 12 months and management intends to maintain a significant buyback rate.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	13.2	20.8	15.5	11.8	10.3	14.1	14.4	31.5	---	35.6	16.8	14.0
Avg. Yld.	0.7%	0.9%	1.0%	1.0%	1.1%	1.1%	0.9%	1.1%	1.4%	1.6%	1.8%	1.5%

Imperial Oil is trading at a price-to-earnings ratio of 16.8. This elevated price-to-earnings ratio is artificially high due to the depressed nature of this year's earnings. If the stock approaches our assumed fair price-to-earnings ratio of 14.0 over the next five years, it will incur a 3.6% annualized drag due to the contraction of its valuation level.

Safety, Quality, Competitive Advantage, & Recession Resiliency

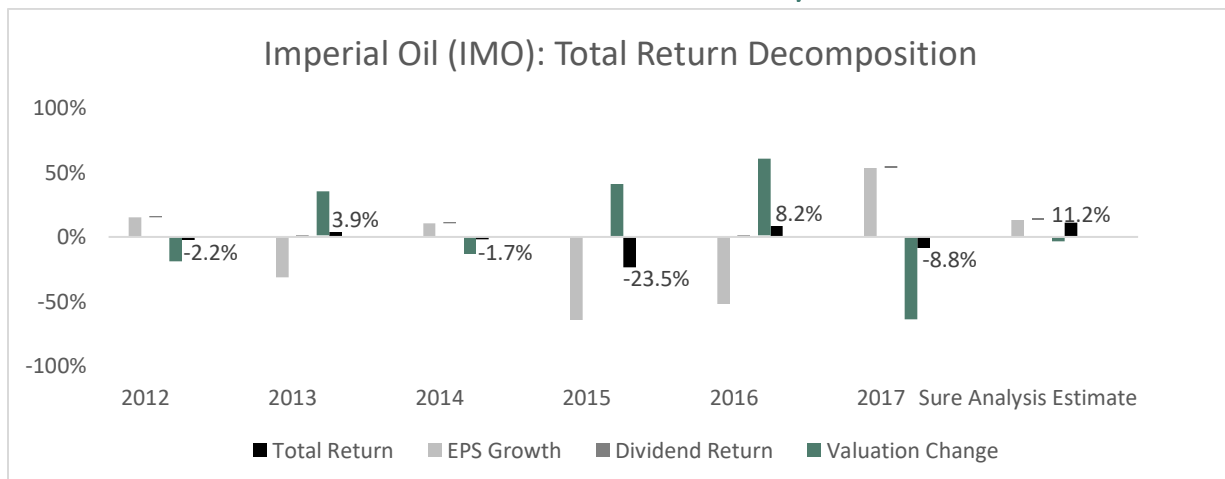
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	56.9%	27.9%	25.4%	27.4%	24.9%	17.1%	18.0%	11.6%	7.5%	7.3%	12.0%	20.0%
Debt/A	46.8%	46.0%	45.7%	47.6%	44.2%	47.5%	44.8%	45.7%	39.9%	41.3%	43.0%	45.0%
Int. Cov.	N/A	441	442	N/A	N/A	340	1255	50	39	8.3	15.0	20.0
Std. Dev.	41.9%	28.7%	19.2%	32.3%	19.9%	14.8%	21.9%	26.8%	20.1%	14.4%	17.0%	17.0%
Payout	8.7%	19.9%	16.1%	11.7%	11.0%	15.4%	13.6%	33.3%	78.6%	58.1%	30.5%	21.4%

Imperial Oil is one of the highest-quality energy businesses in the Canadian market. The company has a credit rating of AA+ from S&P, which is higher than all of its peers in the Canadian energy space. Moreover, the company has paid 100+ years of consecutive dividends and has increased its dividend (in Canadian dollars) for 24 consecutive years. The company's 10-year average dividend growth rate (again, in Canadian dollars) is 6.5%. Imperial Oil seems laser-focused on returning capital to shareholders and we expect this to continue moving forward. Furthermore, the company greatly benefits from leveraging the expertise of its major shareholder, Exxon Mobil.

Final Thoughts & Recommendation

The last several years have been quite difficult for Imperial Oil. Declining oil prices have impacted its profitability and pushed its dividend payout ratio to decade-high levels. With that said, the company's rebound is well underway. We expect the company's earnings to surge over the next five years, which will be partially offset by a revaluation of the company's price-to-earnings multiple. With all this in mind, Imperial Oil appears priced for low double-digit total return. It is certainly a hold, a possibly a buy at current prices – though we'd prefer to buy at or below fair value.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	29739	18745	24186	30819	31062	31777	32818	20963	18915	22473
Gross Profit	7867	4625	5228	6825	7361	5991	6335	3595	2324	2400
Gross Margin	26.5%	24.7%	21.6%	22.1%	23.7%	18.9%	19.3%	17.1%	12.3%	10.7%
SG&A Exp.	978	974	1037	1181	1081	1051	974	875	853	689
Operating Profit	4969	1848	2729	4216	4858	3439	3886	1434	154	279
Op. Margin	16.7%	9.9%	11.3%	13.7%	15.6%	10.8%	11.8%	6.8%	0.8%	1.2%
Net Profit	3652	1390	2143	3409	3767	2746	3428	879	1635	378
Net Margin	12.3%	7.4%	8.9%	11.1%	12.1%	8.6%	10.4%	4.2%	8.6%	1.7%
Free Cash Flow	2855	-611	-629	576	-798	-2918	-802	-648	711	1366
Income Tax	1317	547	721	1047	1227	883	1120	628	211	71

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	13826	16583	20577	24908	29517	34954	35172	31109	30895	33082
Cash & Equivalents	1602	487	267	1177	485	255	185	146	290	950
Acc. Receivable	1181	1627	2000	2243	1986	1957	1326	1139	1500	2157
Inventories	692	770	773	981	1113	1289	1293	1163	1051	1193
Goodwill & Int.	213	249	267	259	261	262	242	161	138	148
Total Liabilities	6469	7625	9401	11860	13055	16618	15764	14229	12337	13651
Accounts Payable	2099	2668	3469	4229	4271	4243	3419	2154	2368	3083
Long-Term Debt	1918	133	756	1160	1520	5784	5792	5696	3448	3697
Total Equity	7357	8958	11175	13048	16462	18336	19408	16881	18558	19431
D/E Ratio	0.26	0.01	0.07	0.09	0.09	0.32	0.30	0.34	0.19	0.19

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	24.2%	9.1%	11.5%	15.0%	13.8%	8.5%	9.8%	2.7%	5.3%	1.2%
Return on Equity	47.8%	17.0%	21.3%	28.1%	25.5%	15.8%	18.2%	4.8%	9.2%	2.0%
ROIC	42.2%	15.1%	20.4%	26.1%	23.4%	13.0%	13.9%	3.7%	7.3%	1.7%
Shares Out.	859.4	847.60	847.60	847.60	847.60	847.60	847.60	847.60	847.60	831.24
Revenue/Share	33.45	21.88	28.31	36.11	36.50	37.36	38.58	24.65	22.24	26.57
FCF/Share	3.21	-0.71	-0.74	0.68	-0.94	-3.43	-0.94	-0.76	0.84	1.61

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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