



Occidental Petroleum Corporation (OXY)

Updated November 6th, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	\$42	5 Year CAGR Estimate:	11.2%	Volatility Percentile:	73.7%
Fair Value Price:	\$31	5 Year Growth Estimate:	12.2%	Momentum Percentile:	2.0%
% Fair Value:	135%	5 Year Valuation Multiple Estimate:	-5.9%	Growth Percentile:	97.6%
Dividend Yield:	7.5%	5 Year Price Target	\$55	Valuation Percentile:	28.6%
Dividend Risk Score:	F	Retirement Suitability Score:	C	Total Return Percentile:	91.5%

Overview & Current Events

Occidental Petroleum is an international oil and gas exploration and production company with operations in the U.S., the Middle East, and Latin America. It has a market capitalization of \$37 billion. While the company also has a midstream and a chemical segment, it is much more sensitive to the price of oil than the integrated oil majors. That's why Occidental was more severely affected than its integrated peers by the downturn in the oil market which began in mid-2014. Due to that downturn, the company reported negligible earnings in 2015 and posted losses in 2016.

On August 8th, Occidental closed the acquisition of Anadarko. Occidental pursued this acquisition thanks to the promising asset base of Anadarko in Permian, which will enhance the already strong presence of Occidental in the area, and the \$3.5 billion annual synergies it expects to achieve from the integration of the two companies. However, this is a huge acquisition, as the \$38 billion value of the deal exceeds the market cap of Occidental. There are great concerns that the deal will stretch the balance sheet of the company to the extreme. Moody's has stated that it will probably downgrade the company from A3 to B-. Occidental has already agreed to sell many non-core assets of Anadarko while it has secured \$10 billion in funding from Berkshire Hathaway (BRK.A) in exchange for preferred shares, which will receive an 8% annual dividend. There are also concerns that Occidental overpaid for the deal. Due to these concerns, the market has punished the stock harshly, sending it to a 10-year low level.

In early November, Occidental reported (11/4/19) financial results for the third quarter of fiscal 2019. Total production reached 1.1 million barrels per day thanks to the acquisition of Anadarko. Legacy Occidental production in the Permian grew 33% over last year's quarter but the total legacy output of the company fell 0.6%. Moreover, average realized oil price fell 4% sequentially. Furthermore, Occidental incurred merger transaction costs and debt financing fees of \$969 million and asset impairment charges of \$325 million. It thus posted a loss of \$912 million. Adjusted earnings-per-share were only \$0.11, as interest expense essentially quadrupled due to the acquisition, from \$96 million in last year's quarter to \$381 million. In addition, management lowered its guidance for next year's production growth from 5% to 2% due to sharp cuts in capital expenses. This move verifies market's concerns over the financial stress that results from the huge acquisition, but more time is required in order to evaluate the merits of the acquisition.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$3.79	\$5.72	\$8.39	\$7.09	\$6.96	\$4.83	\$0.12	-\$1.01	\$0.89	\$5.01	\$2.25	\$4.00
DPS	\$1.30	\$1.42	\$1.76	\$2.07	\$2.45	\$2.80	\$2.94	\$3.01	\$3.05	\$3.10	\$3.14	\$3.34
Shares¹	811.9	812.8	811.0	805.5	796.0	770.6	763.7	764.2	766.4	755.4	846.0	840.0

Due to lackluster oil prices and poor business execution, we have lowered our earnings-per-share estimate for this year from \$3.50 to \$2.25. Moreover, in order to be conservative regarding the dilutive and financial impact of the takeover of Anadarko, we have lowered our forecast for the earnings-per-share in 2024 from \$5.00 to \$4.00. Nevertheless, Occidental has promising growth prospects. It has doubled its output in Permian in the last three years and expects to

¹ In millions

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double it again over the next five years, from 300,000 to 600,000 barrels per day. Investors should realize that our assumed 12.2% average annual earnings-per-share growth rate mostly results from the suppressed earnings of this year.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	17.8	14.4	11.4	12.4	12.8	19.5	---	---	---	15.0	18.7	13.8
Avg. Yld.	1.9%	1.7%	1.8%	3.0%	2.2%	3.0%	4.0%	4.2%	4.7%	4.1%	7.5%	6.1%

In the last 12 months, shares of Occidental have fallen 43%, mostly due to the acquisition of Anadarko. Nevertheless, due to this year's suppressed earnings, Occidental is now trading at a P/E ratio of 18.7, which is higher than its 10-year average P/E ratio of 13.8. If the stock reverts to its average valuation level over the next five years, it will incur a 5.9% annualized drag due to P/E contraction.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	34.3%	24.8%	21.0%	37.0%	27.6%	58.0%	---	---	343%	61.9%	140%	83.5%

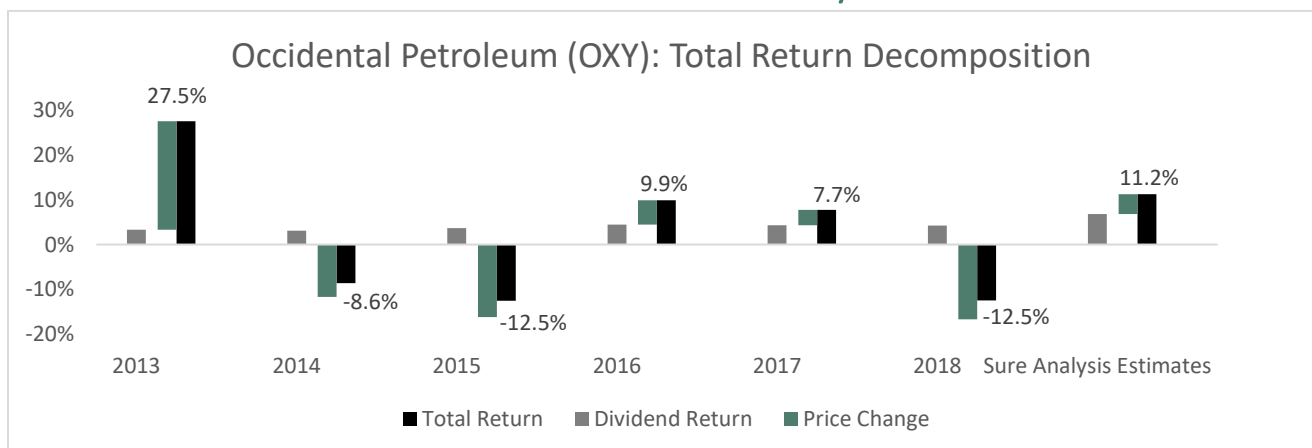
Occidental has raised its dividend for 17 consecutive years at an 11% average annual rate and now offers a generous 7.5% dividend yield. Cash flows are sufficient to support capital expenses and dividends and hence the dividend should be considered safe in the absence of a downturn. On the other hand, Occidental has only marginally raised its dividend in each of the last four years and will almost certainly continue to do so for the foreseeable future, given the Anadarko acquisition. Investors should expect minimal dividend growth and a pause in share repurchases for a few years.

Occidental is remarkably sensitive to the gyrations of oil prices. The company's reliance on oil prices was displayed in the Great Recession, when its earnings-per-share fell 58%, from \$8.98 in 2008 to \$3.79 in 2009. We reiterate that it is much more sensitive to oil prices than the energy sector "supermajors" like Exxon Mobil (XOM) and Total (TOT).

Final Thoughts & Recommendation

Due to its upstream nature and its takeover of Anadarko, which quadrupled interest expense, Occidental is extremely sensitive to the oil price. However, we believe that the market has punished Occidental to the extreme due to its high debt load. In the absence of a downturn in the energy sector, we expect Occidental to reduce its debt load easily thanks to its ample cash flows and offer an 11.2% average annual return over the next five years. We rate the stock as a buy due to its high upside. With that said, the security certainly has an elevated risk profile.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	14942	19045	23939	20100	20170	19312	12480	10090	12508	17824
Gross Profit	9583	12933	16554	13570	13673	12509	6676	4901	6914	11256
Gross Margin	64.1%	67.9%	69.2%	67.5%	67.8%	64.8%	53.5%	48.6%	55.3%	63.2%
SG&A Exp.	1300	1396	1523	1366	1544	1503	1270	1330	1424	1613
Operating Profit	5171	7750	10757	7989	7329	6175	601	-930	1194	5253
Op. Margin	34.6%	40.7%	44.9%	39.7%	36.3%	32.0%	4.8%	-9.2%	9.5%	29.5%
Net Profit	2915	4530	6771	4598	5903	616	-7829	-574	1311	4131
Net Margin	19.5%	23.8%	28.3%	22.9%	29.3%	3.2%	-62.7%	-5.7%	10.5%	23.2%
Free Cash Flow	2562	5626	4763	3438	5570	2680	-2513	552	1519	2749
Income Tax	2063	2995	4201	2659	3214	1685	-1330	-662	17	1477

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	44229	52432	60044	64210	69443	56259	43409	43109	42026	43854
Cash & Equivalents	1224	2578	3781	1592	3393	3789	3201	2233	1672	3033
Acc. Receivable	4092	5032	5395	4916	5674	4206	2970	3989	4145	4893
Inventories	998	1041	1069	1344	1200	1052	986	866	1246	1191
Total Liabilities	15070	19948	22424	24162	26071	21300	19059	21612	21454	22524
Accounts Payable	3282	4646	5304	4708	5520	5229	3069	3926	4408	4885
Long-Term Debt	2796	5111	5871	7623	6939	6838	8305	9819	9828	10317
Total Equity	29081	32484	37620	40016	43126	34959	24350	21497	20572	21330
D/E Ratio	0.10	0.16	0.16	0.19	0.16	0.20	0.34	0.46	0.48	0.48

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.8%	9.4%	12.0%	7.4%	8.8%	1.0%	-15.7%	-1.3%	3.1%	9.6%
Return on Equity	10.3%	14.7%	19.3%	11.8%	14.2%	1.6%	-26.4%	-2.5%	6.2%	19.7%
ROIC	9.4%	13.0%	16.7%	10.1%	12.0%	1.3%	-21.0%	-1.8%	4.2%	13.3%
Shares Out.	811.9	812.8	811.0	805.5	796.0	770.6	763.7	764.2	766.4	755.4
Revenue/Share	18.36	23.40	29.45	24.81	25.07	24.72	16.30	13.21	16.33	23.35
FCF/Share	3.15	6.91	5.86	4.24	6.92	3.43	-3.28	0.72	1.98	3.60

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

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