Marathon Petroleum Corp. (MPC)

Updated January 29th, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	$53	**5 Year CAGR Estimate:**	11.5%	**Market Cap:**	$34.4 B
Fair Value Price:	$74	**5 Year Growth Estimate:**	1.0%	**Ex-Dividend Date:**	2/18/2020
% Fair Value:	72%	**5 Year Valuation Multiple Estimate:**	6.9%	**Dividend Payment Date:**	3/10/2020
Dividend Yield:	4.4%	**5 Year Price Target**	$78	**Years Of Dividend Growth:**	9
Dividend Risk Score:	B	**Retirement Suitability Score:**	A	**Last Dividend Increase:**	9.4%

Overview & Current Events

Marathon Petroleum Corp. (MPC) was spun off from Marathon Oil Corp. (MRO) in 2011. After the acquisition of Andeavor Logistics in October of 2018, MPC has become the largest U.S. refiner, with 16 refineries and a refining capacity of 3.1 million barrels per day. It also has a marketing system that includes ~6,800 branded locations, ~3,900 convenience stores (~2740 are Speedway), and ~1,000 direct dealer locations. In addition, MPC owns a midstream MLP, (MPLX), which has gathering and processing assets as well as pipelines for crude oil and light products. MPLX completed the $9 billion Andeavor acquisition on 7/30/19. Marathon Petroleum Corp. has a market capitalization of $34 billion.

In late January, Marathon Petroleum reported (1/29/20) financial results for the fourth quarter of fiscal 2019. Adjusted earnings-per-share fell -35% over last year's quarter, primarily due to lower fuel margins in the retail segment. That was a notable change over previous quarters. In the year, the retail segment grew its operating income by 54%, mostly thanks to the addition of the Andeavor retail network. In the year, MPC achieved $1.1 billion of synergies from the takeover of Andeavor and thus it exceeded its goal of $600 million by a wide margin. It also continues to aim for $1.4 billion of synergies by the end of 2021.

More importantly, activist investors, including Elliot Management, exerted pressure on MPC for structural changes in an attempt to unlock shareholder value. As a result, MPC will change its CEO and will spin off its Speedway gas station business, probably in the fourth quarter of this year. It will also form a special committee, which will examine ways to unlock value from the midstream business.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	---	$3.34	$4.95	$3.32	$4.39	$5.26	$2.21	$3.77	$6.78	$4.94	***$6.90***	***$7.25***
DPS	---	$0.23	$0.60	$0.77	$0.92	$1.14	$1.36	$1.52	$1.84	$2.12	***$2.32***	***$3.10***
Shares[1]	---	714.0	666.0	594.0	548.0	531.0	528.0	486.0	704.0	653.0	***640.0***	***580.0***

MPC greatly benefits from the inland location of some of the refineries of Andeavor. Thanks to the oil supply glut, these refineries buy their crude oil at a deep discount to WTI, so they enjoy high margins. Furthermore, U.S. refiners will greatly benefit from the new international marine rules, which have come into effect since January 1st, 2020. As per these rules, vessels that sail in international waters are forced to burn diesel instead of heavy fuel oil. As the former is much more expensive than the latter, it should boost refiner earnings. MPC is properly positioned to benefit from the new marine rules. Thanks to a series of past investments, the refiner can upgrade about 600,000 barrels per day of low-value residue to diesel. Given all the above factors, we believe that MPC can grow its earnings-per-share by 40% this year, from $4.94 in 2019 to $6.90. As the effect of the new marine standard will be a major growth driver only this year, we expect just 1% annual earnings-per-share growth beyond this year, just to be on the safe side.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	---	5.4	4.7	11.6	10.0	9.6	18.2	14.4	10.8	11.8	***7.7***	***10.7***
Avg. Yld.	---	1.3%	2.6%	2.0%	2.1%	2.3%	3.4%	2.8%	2.5%	3.6%	***4.4%***	***4.0%***

[1] In millions of shares

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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Marathon is now trading at a forward price-to-earnings ratio of 7.7, which is much lower than its historical average of 10.7. If the stock reverts to its average earnings multiple over the next five years, it will enjoy a 6.9% annualized gain in its return thanks to its markedly cheap valuation right now.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	6.9%	12.1%	23.2%	21.0%	21.7%	61.5%	40.3%	34.8%	42.9%	***33.6%***	***42.8%***

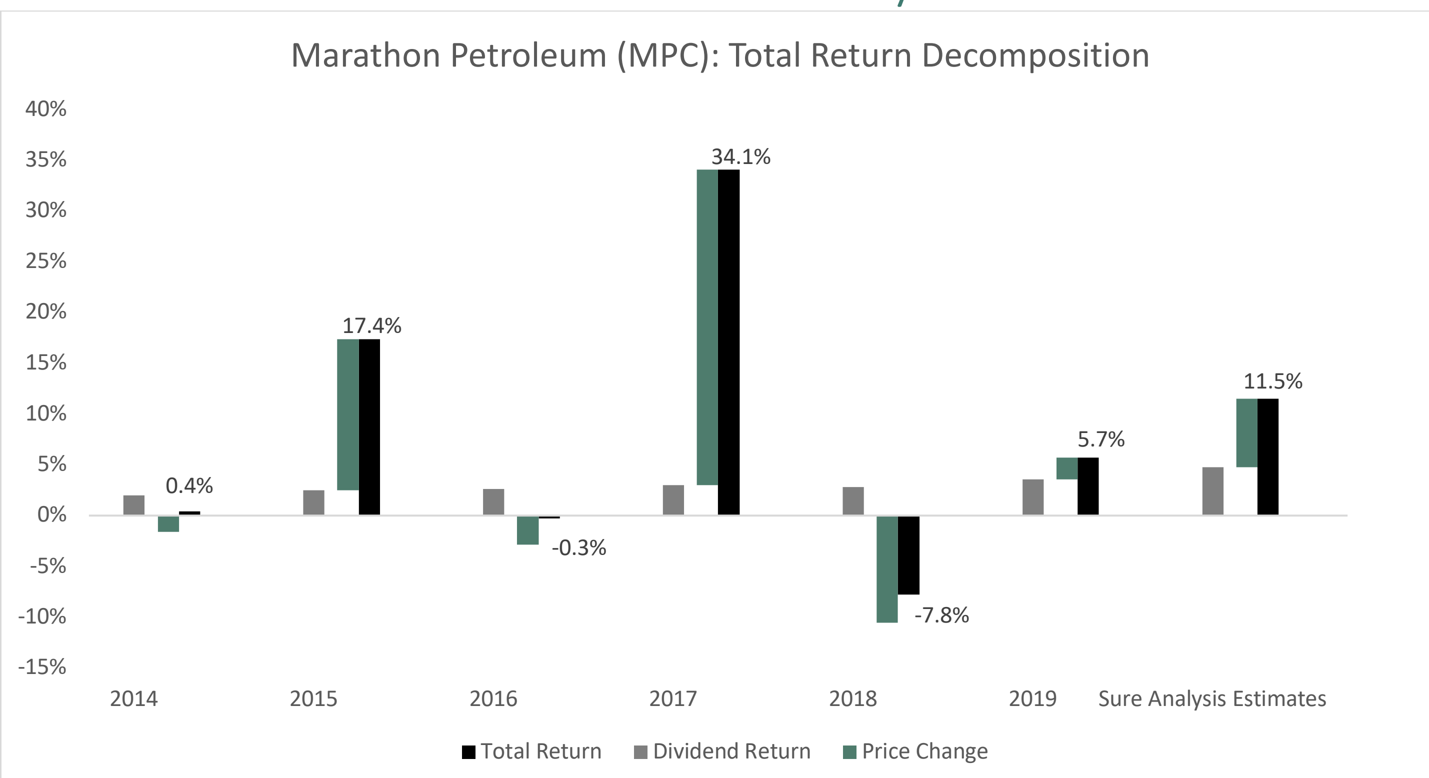
The acquisition of Andeavor has greatly enhanced the geographic diversification of Marathon and its potential to take advantage of fluctuations in price spreads among different types of crude oil and the dynamics of export markets. The acquisition will thus increase the earnings of the company and its resilience during downturns.

On the other hand, refining is a highly cyclical business, hence refiners are vulnerable to recessions. This was evident in the Great Recession, when the demand for oil products deteriorated and refining margins plunged.

Final Thoughts & Recommendation

Thanks to the market's enthusiasm over the structural changes triggered by activist investors and the new international marine standard, MPC rallied 50% in about two months, in early fall. Since then, the stock has corrected -22% and hence it become attractive again. We expect the stock to offer an 11.5% average annual return over the next five years, thanks to a 6.9% annualized expansion of its valuation level, its 4.4% dividend and 1% annual earnings-per-share growth. We thus rate it as a buy at its current price. While the highly cyclical nature of the refining business is always a risk factor, the stock seems exceptionally cheap right now.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	62487	78638	82243	100B	97817	72051	63339	74733	96504	
Gross Profit	8163	10927	13295	12402	13542	15790	6524	7644	10438	
Gross Margin	13.1%	13.9%	16.2%	12.4%	13.8%	21.9%	10.3%	10.2%	10.8%	
SG&A Exp.	874	1059	1223	1248	1375	1576	1597	1694	2418	
D&A Exp.	941	891	995	1220	1326	1502	2001	2114	2490	
Operating Profit	930	3683	5144	3383	3877	4741	2669	3702	5175	
Op. Margin	1.5%	4.7%	6.3%	3.4%	4.0%	6.6%	4.2%	5.0%	5.4%	
Net Profit	623	2389	3389	2112	2524	2852	1215	3497	2855	
Net Margin	1.0%	3.0%	4.1%	2.1%	2.6%	4.0%	1.9%	4.7%	3.0%	
Free Cash Flow	1000	2124	3123	2199	1630	2075	1125	3880	2580	
Income Tax	400	1330	1845	1113	1280	1506	609	-460	962	

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	23232	25745	27223	28385	30425	43115	44413	49047	92940	
Cash & Equivalents	118	3079	4860	2292	1494	1127	887	3011	1687	
Acc. Receivable	N/A	5461	4610	5559	4058	2927	3617	4695	5853	
Inventories	3071	3320	3449	4689	5642	5225	5656	5550	9837	
Goodwill & Int.	837	842	930	938	1566	4019	3587	4217	23498	
Total Liabilities	14988	16240	15118	17053	19035	23440	24210	28219	48891	
Accounts Payable	6453	8189	6785	8234	6661	4743	5593	8297	9366	
Long-Term Debt	3897	3307	3361	3396	6602	11925	10572	12946	27524	
Total Equity	8244	9505	11694	10920	10751	13237	13557	14033	35175	
D/E Ratio	0.47	0.35	0.29	0.31	0.61	0.90	0.78	0.92	0.78	

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.8%	9.8%	12.8%	7.6%	8.6%	7.8%	2.8%	7.5%	4.0%	
Return on Equity	7.2%	26.9%	32.0%	18.7%	23.3%	23.8%	9.1%	25.3%	11.6%	
ROIC	5.2%	19.1%	24.0%	14.0%	15.4%	11.5%	3.9%	10.8%	5.4%	
Shares Out.	---	714.0	666.0	594.0	548.0	531.0	528.0	486.0	704.0	
Revenue/Share	87.27	110.14	120.24	157.98	170.41	132.94	119.51	145.96	183.47	
FCF/Share	1.40	2.97	4.57	3.47	2.84	3.83	2.12	7.58	4.90	

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