



Phillips 66 (PSX)

Updated February 3rd, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	\$91	5 Year CAGR Estimate:	11.3%	Market Cap:	\$40.1 B
Fair Value Price:	\$120	5 Year Growth Estimate:	2.0%	Ex-Dividend Date:	2/13/2020 ¹
% Fair Value:	76%	5 Year Valuation Multiple Estimate:	5.7%	Dividend Payment Date:	2/28/2020
Dividend Yield:	4.3%	5 Year Price Target	\$132	Years Of Dividend Growth:	7
Dividend Risk Score:	C	Retirement Suitability Score:	B	Last Dividend Increase:	12.5%

Overview & Current Events

Phillips 66 was spun off from ConocoPhillips in 2012. Phillips 66 has a market capitalization of \$40 billion and operates in four segments: refining, midstream, chemicals, and marketing. It is a diversified company with each of its segments behaving differently under various oil prices. When oil prices began to collapse in 2014, the refining segment became by far the most profitable segment, as low oil prices improved demand for oil products and boosted refining margins. In 2019, the refining segment generated 48% of the total earnings of Phillips 66.

In late January, Phillips 66 reported (1/31/20) financial results for the fourth quarter of fiscal 2019. Adjusted earnings fell -51% sequentially, from \$1.4 billion to \$689 million, due to low margins amid unfavorable seasonality in the refining and marketing segments. The midstream segment was the bright exception, as its adjusted pre-tax profit fell only -8% sequentially thanks to the transportation and NGL businesses, which posted record results in the full year.

Phillips 66 missed analysts' earnings-per-share estimates for the first time in 10 quarters. Since 2012, the stock has returned \$26 billion (65% of its current market cap) to its shareholders in dividends and share repurchases.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	---	---	\$6.48	\$5.92	\$7.10	\$7.73	\$2.92	\$4.58	\$11.85	\$8.05	\$10.00	\$11.04
DPS	---	---	\$0.45	\$1.33	\$1.89	\$2.18	\$2.45	\$2.73	\$3.10	\$3.50	\$3.90	\$5.00
Shares²	---	---	637	619	571	547	530	519	464	441	420	340

Growth projects in the oil industry take many years to start bearing fruit and hence there is a great lag between capital expenses and their resultant cash flows. Fortunately for the shareholders of Phillips 66, the company is currently in the positive phase of its cycle. While it has greatly reduced its capital expenses in recent years, it has begun to reap the benefits from its huge investments in 2014 and 2015, when it invested a total of \$9.5 billion. In addition, management is well known for its discipline to invest only in high-return projects.

Phillips 66 will greatly benefit from the new international marine standard (IMO 2020), which has forced vessels sailing in international waters to burn low-sulfur diesel instead of heavy fuel oil since January 1st, 2020. Diesel is much more expensive than fuel oil and hence refiners will enjoy a boost in their earnings. Phillips 66 also has many ongoing growth projects in its midstream segment. This segment remained resilient in the adverse fourth quarter and is likely to have an increasing contribution to the total results in the upcoming years. Moreover, Phillips 66 has repurchased its shares at a -5% average annual rate in the last six years and has confirmed its intention to continue to repurchase its shares at a similar pace.

We expect Phillips 66 to grow its earnings-per-share 24% this year, mostly thanks to IMO 2020, and 2% per year on average beyond this year, thanks to the other aforementioned growth drivers. As this year will form a high comparison base for future years, we find it prudent to assume only 2.0% earnings-per-share growth beyond this year.

¹ Estimated date.

² In millions.

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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	---	---	6.4	10.5	11.1	10.3	27.7	18.5	8.9	12.4	9.1	12.0
Avg. Yld.	---	---	1.1%	2.1%	2.4%	2.7%	3.0%	3.2%	2.9%	3.5%	4.3%	3.8%

Phillips 66 is now trading at a price-to-earnings ratio of 9.1, which is lower than its 10-year average of 13.2. In order to be conservative, we assume a fair earnings multiple of 12.0 for this stock. If the stock approaches our fair value estimate within the next five years, it will enjoy a 5.7% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

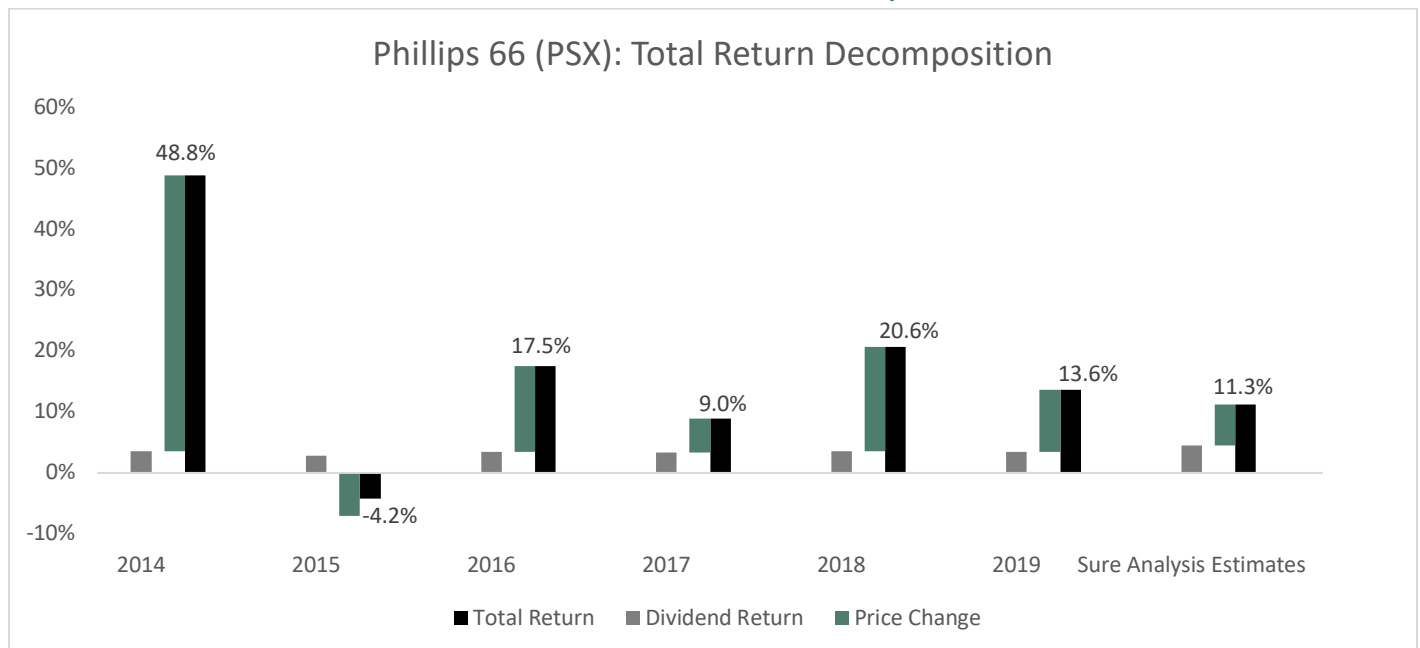
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	6.9%	22.5%	26.6%	28.2%	83.9%	59.6%	26.2%	43.5%	39.0%	45.3%

Phillips 66 has a significant competitive advantage, namely the discipline of its management to invest only in high-return projects. However, despite its diversified business, the company is cyclical, just like most oil companies. In the recent downturn of the oil sector, between mid-2014 and 2017, low oil prices resulted in high refining margins thanks to healthy underlying economic growth. However, in the Great Recession, the price of oil products plunged along with the price of oil and resulted in low refining margins. Phillips 66 will have significant downside risk in such an event.

Final Thoughts & Recommendation

Phillips 66 is a well-managed company, which is properly positioned for most scenarios of oil prices. Moreover, the stock has incurred a -24% correction in the last three months, primarily due to the massive sell-off of the entire energy sector, which has been caused by the threat of coronavirus. As a result, Phillips 66 has become remarkably attractive. We expect the stock to offer an 11.3% average annual return over the next five years thanks to its 4.3% dividend yield, 2.0% annual earnings-per-share growth and a 5.7% annualized expansion of its valuation level. We thus rate it as a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue (\$B)	146.6	195.9	179.3	171.6	161.2	99.0	84.3	102.4	111.5	
Gross Profit	21469	23163	24877	23351	25464	25576	21811	22945	13531	
Gross Margin	14.6%	11.8%	13.9%	13.6%	15.8%	25.8%	25.9%	22.4%	12.1%	
SG&A Exp.	1384	1394	1703	1478	1663	1670	1638	1695	1677	
D&A Exp.	880	902	906	947	995	1078	1168	1318	1356	
Operating Profit	1078	2521	4612	2666	3430	4548	1098	1838	5209	
Op. Margin	0.7%	1.3%	2.6%	1.6%	2.1%	4.6%	1.3%	1.8%	4.7%	
Net Profit	735	4775	4124	3726	4762	4227	1555	5106	5595	
Net Margin	0.5%	2.4%	2.3%	2.2%	3.0%	4.3%	1.8%	5.0%	5.0%	
Free Cash Flow	942	3990	2595	4248	-244	-51	119	1816	4934	
Income Tax	579	1822	2473	1844	1654	1764	547	-1693	1572	

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	44955	43211	48073	49798	48692	48580	51653	54371	54302	
Cash & Equivalents	0	0	3474	5400	5207	3074	2711	3119	3019	
Acc. Receivable	8364	10025	10403	9632	7255	5173	6397	7506	6173	
Inventories	4113	3466	3430	3354	3397	3477	3150	3395	3543	
Goodwill & Int.	4410	4064	4068	3794	4174	4181	4158	4146	4139	
Total Liabilities	18929	19918	27267	27406	26655	24642	27928	26943	27149	
Accounts Payable	9814	10792	10710	11090	8064	5655	7061	8027	6586	
Long-Term Debt	417	391	6974	6155	8635	8887	10138	10110	11160	
Total Equity	26001	23264	20775	21950	21590	23100	22390	25085	24653	
D/E Ratio	0.02	0.02	0.34	0.28	0.40	0.38	0.45	0.40	0.45	

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	1.7%	10.8%	9.0%	7.6%	9.7%	8.7%	3.1%	9.6%	10.3%	
Return on Equity	2.8%	19.4%	18.7%	17.4%	21.9%	18.9%	6.8%	21.5%	22.5%	
ROIC	2.7%	19.1%	16.0%	13.2%	16.1%	13.3%	4.7%	14.3%	14.8%	
Shares Out.	---	---	636.76	618.99	571.50	546.98	530.07	518.51	464.4	
Revenue/Share	229.00	306.14	281.56	277.22	282.08	180.95	159.00	197.40	235.13	
FCF/Share	1.47	6.23	4.08	6.86	-0.43	-0.09	0.22	3.50	10.41	

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

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