Marathon Petroleum Corp. (MPC)

Updated May 13th, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	$32	**5 Year CAGR Estimate:**	16.8%	**Market Cap:**	$21.3 B
Fair Value Price:	$49	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	5/19/2020
% Fair Value:	65%	**5 Year Valuation Multiple Estimate:**	8.9%	**Dividend Payment Date:**	6/10/2020
Dividend Yield:	7.3%	**5 Year Price Target**	$57	**Years Of Dividend Growth:**	9
Dividend Risk Score:	F	**Retirement Suitability Score:**	D	**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 (~2,740 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. Marathon Petroleum Corp. has a market capitalization of $21.3 billion.

MPC is currently facing a severe downturn due to the coronavirus, which has caused a collapse in the global demand for refined products, particularly jet fuel and gasoline. As a result, the spin-off the Speedway gas station business has been delayed. Management still aims to spin off the business in the fourth quarter but it is not likely to meet its deadline. The current market cap of the stock, which is only slightly higher than the expected sale price of Speedway ($15-$20 billion) shows that the market does not expect the spin-off to materialize anytime soon. We expect the spin-off to materialize next year and unlock great value for the shareholders who can remain patient.

In early May, Marathon Petroleum reported (5/5/20) financial results for the first quarter of fiscal 2020. Due to the collapse of the oil price, the company posted asset impairments of $12.4 billion. Excluding these charges, MPC widened its adjusted loss per share from -$0.09 in last year's quarter to -$0.16. The retail and midstream segments performed well but the refining segment widened its operating loss from -$334 million to -$622 million due to lower refining margins and higher planned maintenance costs. Nevertheless, investors should keep in mind that the first quarter is always a weak quarter from a seasonality point of view due to weak demand for gasoline and jet fuel.

Due to the collapse in the demand for refined products caused by the pandemic, MPC reduced the utilization rate of its refineries to minimum (50%-65%) in April, just like the other refiners. We expect MPC to lose -$1.80 per share this year. On the bright side, demand for gasoline has improved in May and will improve further when the pandemic subsides.

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	***-$1.80***	***$5.32***
DPS	---	$0.23	$0.60	$0.77	$0.92	$1.14	$1.36	$1.52	$1.84	$2.12	***$2.32***	***$2.69***
Shares[1]	---	714.0	666.0	594.0	548.0	531.0	528.0	486.0	704.0	653.0	***648.0***	***610.0***

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, when the pandemic subsides, 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 or ultra-low sulfur fuel oil instead of heavy fuel oil. As the former are much more expensive than the latter, they 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. We expect the pandemic to subside and the demand for oil products to recover from next year. We expect MPC to grow its earnings-per-share by 3.0% per year on average off their mid-cycle level (5-year average) of $4.59.

[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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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	***7.0***	***10.7***
Avg. Yld.	---	1.3%	2.6%	2.0%	2.1%	2.3%	3.4%	2.8%	2.5%	3.6%	***7.3%***	***4.7%***

Marathon is now trading at 7.0 times its mid-cycle earnings-per-share of $4.59. This valuation level 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 an 8.9% annualized gain in its return.

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%	***50.5%***	***50.5%***

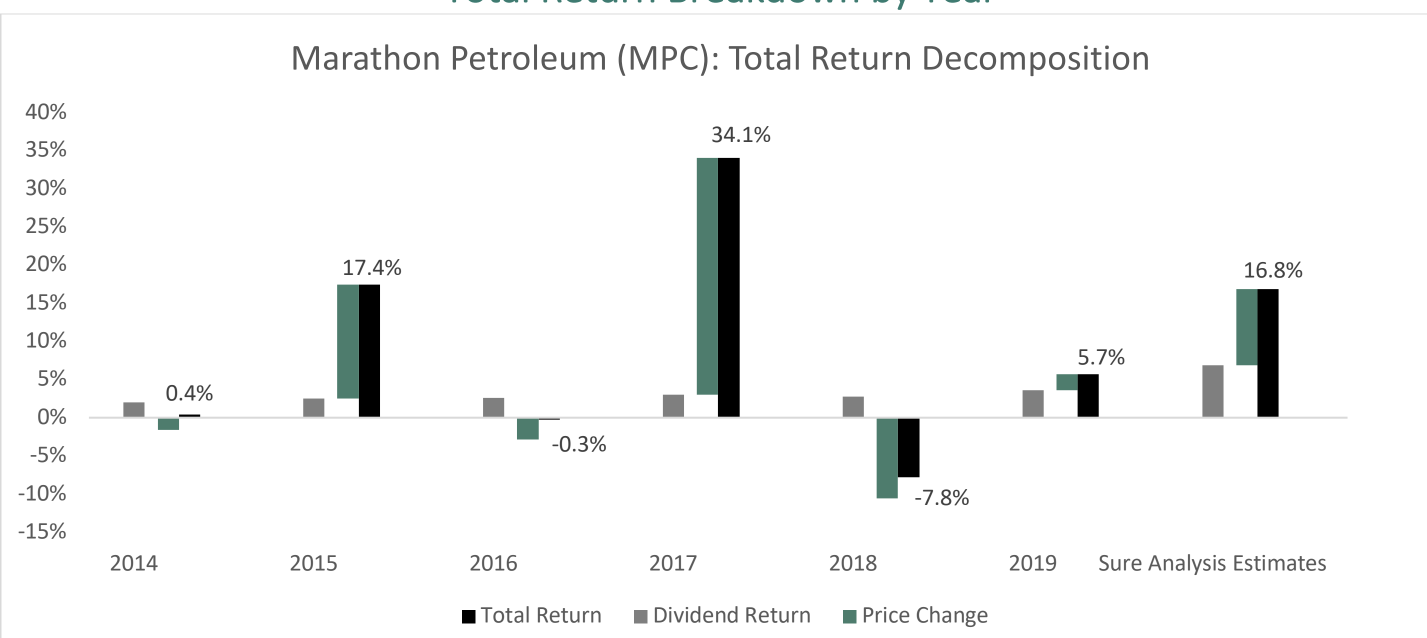
The acquisition of Andeavor has greatly enhanced the geographic diversification of Marathon and its potential to take advantage of fluctuations in price spreads among different types of crude oil and the dynamics of export markets. The acquisition will thus increase the earnings of the company and its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

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. MPC has been caught with a significant amount of debt in the current downturn due to its acquisition of Andeavor. Its interest expense consumes 40% of operating income while its net debt of $46.8 billion is about 16 times its annual earnings.

Final Thoughts & Recommendation

Due to its acquisition of Andeavor, MPC has been caught with a significant amount of debt in the ongoing downturn, which has been caused by the coronavirus. However, we expect the pandemic to subside from next year and the refiner to endure the downturn thanks to its reduced expenses and the recent issuance of bonds. As the stock has fallen -47% in less than three months, it has become markedly cheap and could offer a 16.8% average annual return over the next five years. The stock thus earns a buy rating. Investors who are afraid that the pandemic may last beyond next year may prefer a company like HollyFrontier, which has a much stronger balance sheet than MPC.

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	100160	97817	72051	63339	74733	96504	123949
Gross Profit	7,222	10,036	12,300	11,182	12,216	14,288	4,523	5,530	7,948	10,068
Gross Margin	11.6%	12.8%	15.0%	11.2%	12.5%	19.8%	7.1%	7.4%	8.2%	8.1%
SG&A Exp.	874	1,059	1,223	1,248	1,375	1,576	1,597	1,694	2,418	3,408
D&A Exp.	941	891	995	1,220	1,326	1,502	2,001	2,114	2,490	3,638
Operating Profit	930	3,683	5,144	3,383	3,877	4,741	2,669	3,702	5,175	6,072
Op. Margin	1.5%	4.7%	6.3%	3.4%	4.0%	6.6%	4.2%	5.0%	5.4%	4.9%
Net Profit	623	2,389	3,389	2,112	2,524	2,852	1,174	3,432	2,780	2,637
Net Margin	1.0%	3.0%	4.1%	2.1%	2.6%	4.0%	1.9%	4.6%	2.9%	2.1%
Free Cash Flow	1,000	2,124	3,123	2,199	1,630	2,075	1,125	3,880	2,580	4,067
Income Tax	400	1,330	1,845	1,113	1,280	1,506	609	(460)	962	1,074

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	98,556
Cash & Equivalents	118	3079	4860	2292	1494	1127	887	3011	1687	1,527
Acc. Receivable	N/A	5461	4610	5559	4058	2927	3617	4695	5853	7,872
Inventories	3071	3320	3449	4689	5642	5225	5656	5550	9837	10,243
Goodwill & Int.	837	842	930	938	1566	4019	3587	4217	23498	22,968
Total Liabilities	14988	16240	15118	17053	19035	23440	24210	28219	48891	56,417
Accounts Payable	6453	8189	6785	8234	6661	4743	5593	8297	9366	11,623
Long-Term Debt	3897	3307	3361	3396	6602	11925	10572	12946	27524	28,838
Total Equity	8244	9505	11694	10920	10751	13237	13557	14033	35175	33,694
D/E Ratio	0.47	0.35	0.29	0.31	0.61	0.90	0.78	0.92	0.78	0.86

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%	2.7%	7.3%	3.9%	2.8%
Return on Equity	7.2%	26.9%	32.0%	18.7%	23.3%	23.8%	8.8%	24.9%	11.3%	7.7%
ROIC	5.2%	19.1%	24.0%	14.0%	15.4%	11.5%	3.8%	10.6%	5.3%	3.7%
Shares Out.	---	714.0	666.0	594.0	548.0	531.0	528.0	486.0	704.0	653.0
Revenue/Share	87.27	110.14	120.24	157.98	170.41	132.94	119.51	145.96	183.47	186.67
FCF/Share	1.40	2.97	4.57	3.47	2.84	3.83	2.12	7.58	4.90	6.13

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