



Phillips 66 (PSX)

Updated February 1st, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	\$68	5 Year CAGR Estimate:	11.3%	Market Cap:	\$30.0 B
Fair Value Price:	\$84	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	2/12/2021 ¹
% Fair Value:	81%	5 Year Valuation Multiple Estimate:	4.4%	Dividend Payment Date:	2/28/2021
Dividend Yield:	5.3%	5 Year Price Target	\$98	Years Of Dividend Growth:	8
Dividend Risk Score:	F	Retirement Suitability Score:	D	Last Dividend Increase:	2.9%

Overview & Current Events

Phillips 66 was spun off from ConocoPhillips in 2012. Phillips 66 has a market capitalization of \$30 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, in the absence of a severe recession. When oil prices collapsed 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 (1/29/21) financial results for the fourth quarter of fiscal 2020. The pandemic took its toll on the marketing segment while it continues to weigh heavily on the refining segment, which widened its pre-tax loss sequentially, from -\$970 million to -\$1.09 billion. As a result, the company posted an adjusted loss of -\$1.16 per share and thus missed analysts' consensus by \$0.16. The refining segment has been severely hurt, not only by the collapse in the demand for refined products due to the pandemic, but also by the aggressive production cuts of OPEC and Russia, which have boosted the price of oil and thus the input cost of refiners. Nevertheless, we expect the pandemic to subside in the second half of this year and we expect Phillips 66 to earn \$2.50 per share this year. Moreover, the minor loss of -\$0.89 per share in 2020 is a testament to the diversified business model of Phillips 66.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	---	\$6.48	\$5.92	\$7.10	\$7.73	\$2.92	\$4.58	\$11.85	\$8.05	-\$0.89	\$2.50	\$8.15
DPS	---	\$0.45	\$1.33	\$1.89	\$2.18	\$2.45	\$2.73	\$3.10	\$3.50	\$3.60	\$3.60	\$3.80
Shares²	---	637	619	571	547	530	519	464	441	439	439	400

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.

The pandemic greatly affected the results of Phillips 66 last year but we expect the company to recover later this year, along with the energy market. In order to calculate its future returns, we have used its mid-cycle (5-year average) earnings-per-share of \$7.03 as a base. As soon as the pandemic subsides, Phillips 66 will 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. Phillips 66 also has many ongoing growth projects in its midstream segment. Moreover, while Phillips 66 has suspended share repurchases due to the pandemic, it will resume them when the economy recovers. Overall, we expect Phillips 66 to grow its earnings-per-share by 3.0% per year on average over the next five years off its mid-cycle level.

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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	---	6.4	10.5	11.1	10.3	27.7	18.5	8.9	12.4	---	9.7	12.0
Avg. Yld.	---	1.1%	2.1%	2.4%	2.7%	3.0%	3.2%	2.9%	3.5%	5.3%	5.3%	3.9%

Phillips 66 is now trading at 9.7 times its mid-cycle earnings. This valuation level 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 4.4% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

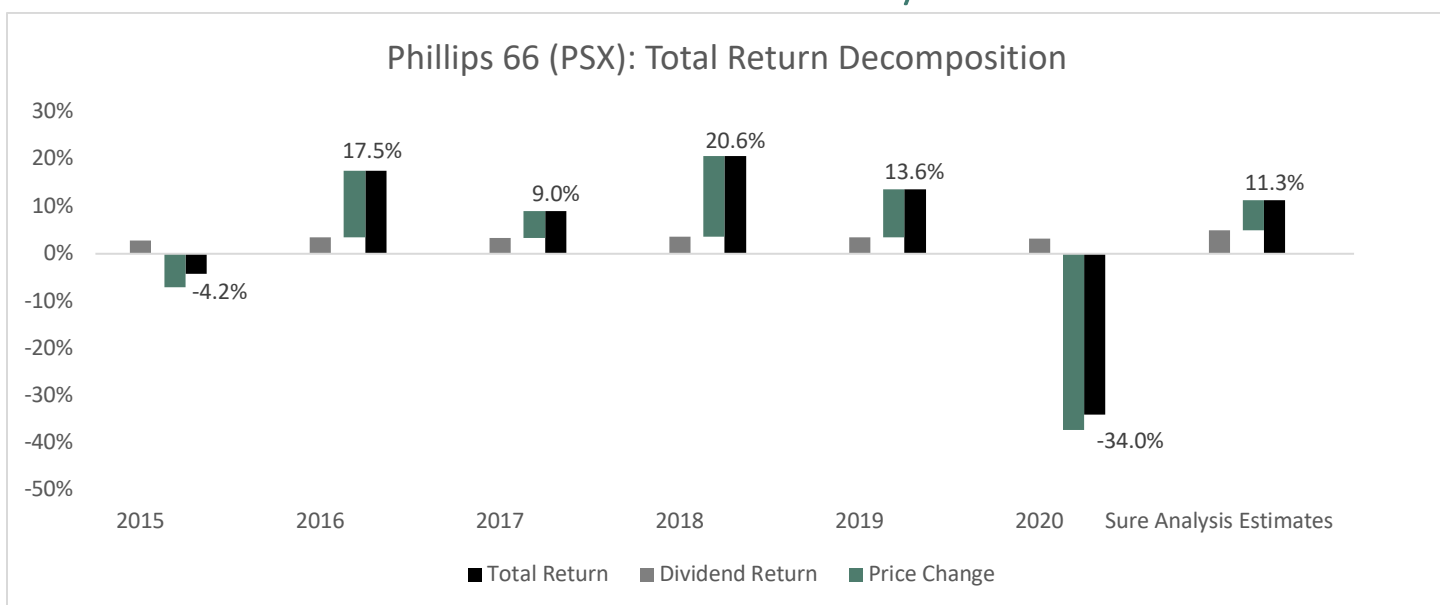
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	6.9%	22.5%	26.6%	28.2%	83.9%	59.6%	26.2%	43.5%	---	51.2%	46.7%

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. The current downturn is much fiercer than the recent downturn and hence it forced Phillips 66 to post its first annual loss in its 9-year history.

Final Thoughts & Recommendation

Phillips 66 is a well-managed company, properly positioned for most scenarios of oil prices, but it is now facing a severe downturn due to the pandemic. Nevertheless, thanks to the distribution of vaccines, the pandemic may subside in the second half of the year. This expectation has led Phillips 66 to rally 42% since our last research report, in November. While the stock has become less attractive, it could still offer an 11.3% average annual return over the next five years. We thus withdraw our “strong buy” rating but we still rate the stock as a “buy” for those who can wait patiently for the recovery of the energy market.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue (\$B)	195.9	179.3	171.6	161.2	99.0	84.3	102.4	111.4	107.3
Gross Profit	23,163	24,877	23,351	25,464	25,576	21,811	22,945	13,531	11,764
Gross Margin	11.8%	13.9%	13.6%	15.8%	25.8%	25.9%	22.4%	12.1%	11.0%
SG&A Exp.	1,394	1,703	1,478	1,663	1,670	1,638	1,695	1,677	1,681
D&A Exp.	902	906	947	995	1,078	1,168	1,318	1,356	1,341
Operating Profit	2,521	4,612	2,666	3,430	4,548	1,098	1,838	5,209	3,335
Op. Margin	1.3%	2.6%	1.6%	2.1%	4.6%	1.3%	1.8%	4.7%	3.1%
Net Profit	4,775	4,124	3,726	4,762	4,227	1,555	5,106	5,595	3,076
Net Margin	2.4%	2.3%	2.2%	3.0%	4.3%	1.8%	5.0%	5.0%	2.9%
Free Cash Flow	3,990	2,595	4,248	(244)	(51)	119	1,816	4,934	935
Income Tax	1,822	2,473	1,844	1,654	1,764	547	(1,693)	1,572	801

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	43,211	48,073	49,798	48,692	48,580	51,653	54,371	54,302	58,720
Cash & Equivalents	-	3,474	5,400	5,207	3,074	2,711	3,119	3,019	1,614
Acc. Receivable	10,025	10,403	9,632	7,255	5,173	6,397	7,506	6,173	8,510
Inventories	3,466	3,430	3,354	3,397	3,477	3,150	3,395	3,543	3,776
Goodwill & Int.	4,064	4,068	3,794	4,174	4,181	4,158	4,146	4,139	4,139
Total Liabilities	19,918	27,267	27,406	26,655	24,642	27,928	26,943	27,149	31,551
Accounts Payable	10,792	10,710	11,090	8,064	5,655	7,061	8,027	6,586	8,575
Long-Term Debt	391	6,974	6,155	8,635	8,887	10,138	10,110	11,160	11,763
Total Equity	23,264	20,775	21,950	21,590	23,100	22,390	25,085	24,653	24,910
D/E Ratio	0.02	0.34	0.28	0.40	0.38	0.45	0.40	0.45	0.47

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	10.8%	9.0%	7.6%	9.7%	8.7%	3.1%	9.6%	10.3%	5.4%
Return on Equity	19.4%	18.7%	17.4%	21.9%	18.9%	6.8%	21.5%	22.5%	12.4%
ROIC	19.1%	16.0%	13.2%	16.1%	13.3%	4.7%	14.3%	14.8%	8.0%
Shares Out.	---	637	619	571	547	530	519	464	441
Revenue/Share	306.14	281.56	277.22	282.08	180.95	159.00	197.40	235.13	236.39
FCF/Share	6.23	4.08	6.86	(0.43)	(0.09)	0.22	3.50	10.41	2.06

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

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