ConocoPhillips (COP)

Updated May 9th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	$108	**5 Year CAGR Estimate:**	-1.0%	**Market Cap:**	$139.3 B
Fair Value Price:	$165	**5 Year Growth Estimate:**	-11.0%	**Ex-Dividend Date:**	5/16/2022
% Fair Value:	65%	**5 Year Valuation Multiple Estimate:**	8.8%	**Dividend Payment Date:**	6/1/2022
Dividend Yield:	1.7%	**5 Year Price Target**	$92	**Years Of Dividend Growth:**	6
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Sell

Overview & Current Events

ConocoPhillips is the world's largest independent oil and gas producer, with a production of 1.7 million barrels per day and a market capitalization of $139.3 billion. The company was founded in 2002 and is headquartered in Houston, Texas.

On January 15th, 2021, ConocoPhillips closed the acquisition of Concho Resources for $9.7 billion in an all-stock deal. This was the largest shale oil deal in 2020. ConocoPhillips pursued this deal thanks to the low production cost of Concho and the high rate of return of this deal.

On September 21st, 2021, ConocoPhillips announced its agreement to buy Shell's Permian Basin assets for $9.5 billion in cash. The deal will increase the Permian output of ConocoPhillips by 40% and will result in great synergies, as the company will become the second-largest producer in the Permian, behind only Pioneer Natural Resources (PXD).

In early May, ConocoPhillips reported (5/5/22) financial results for the first quarter of fiscal 2022. As ConocoPhillips is a pure upstream company that does not hedge its output, it greatly benefited from the rally of the oil price to a 13-year high due to the sanctions of western countries on Russia. The average realized oil price jumped 70% over last year's quarter and thus the company more than quadrupled its earnings-per-share, from $0.69 to $3.27. Thanks to its pure upstream nature, ConocoPhillips outperformed its integrated peers Exxon and Chevron by a wide margin. Moreover, the oil price is likely to remain excessive this year, as oil producers are reluctant to boost their output due to their concerns over the secular shift of the world from fossil fuels to clean energy sources. Given the impact of the war on oil prices, we have raised our forecast for earnings-per-share in 2022 from $9.00 (our forecast before the war) to $13.20. On the other hand, we expect oil producers to boost their output at some point beyond this year and thus drive the oil price lower.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$5.91	$6.43	$4.96	-$1.39	-$2.52	$0.61	$4.54	$3.59	-$0.97	$6.01	***$13.20***	***$7.37***
DPS	$2.64	$2.70	$2.84	$2.94	$1.00	$1.06	$1.16	$1.33	$1.69	$1.75	***$1.84***	***$2.24***
Shares[1]	1220	1230	1230	1240	1240	1180	1140	1100	1074	1321	***1300***	***1200***

When oil prices began to collapse in 2014, ConocoPhillips was, among the large oil companies, the producer that suffered the most. The company posted heavy losses in 2015 and 2016 and its stock price fell -60% from its peak. However, the company seems to have learned its lesson. It has focused on high grading its asset portfolio with the addition of low-cost barrels in order to achieve positive free cash flows even at oil prices below $40.

Unfortunately, the company has posted flat production in the last two years due to the pandemic and the natural decline of its fields. In addition, it has posted an organic reserve replacement ratio of only 66.5% in the last two years.

Nevertheless, the company is thriving right now thanks to 13-year high oil prices. Moreover, the huge acquisitions of low-cost reserves in the Permian have proved highly profitable. We also expect a decrease in interest expense to continue to support earnings growth. On the other hand, due to the high comparison base formed by the record earnings expected this year, we expect earnings-per-share to decline -11% per year on average over the next five years.

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[1] In millions.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	9.5	10.1	15.0	---	---	---	13.7	17.1	---	9.8	***8.2***	***12.5***
Avg. Yld.	4.7%	4.2%	3.8%	5.1%	2.4%	2.2%	1.9%	2.2%	4.1%	3.0%	***1.7%***	***2.4%***

ConocoPhillips is currently trading at a 10-year low price-to-earnings ratio of 8.2 due to its blowout earnings. We have assumed a fair price-to-earnings ratio of 12.5 for 2027, which is the average earnings multiple over the last decade. If this turns out to be correct, the stock will enjoy an 8.8% annualized valuation gain in its returns over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	44.7%	42.0%	57.3%	---	---	174%	25.6%	37.0%	---	29.1%	***13.9%***	***30.4%***

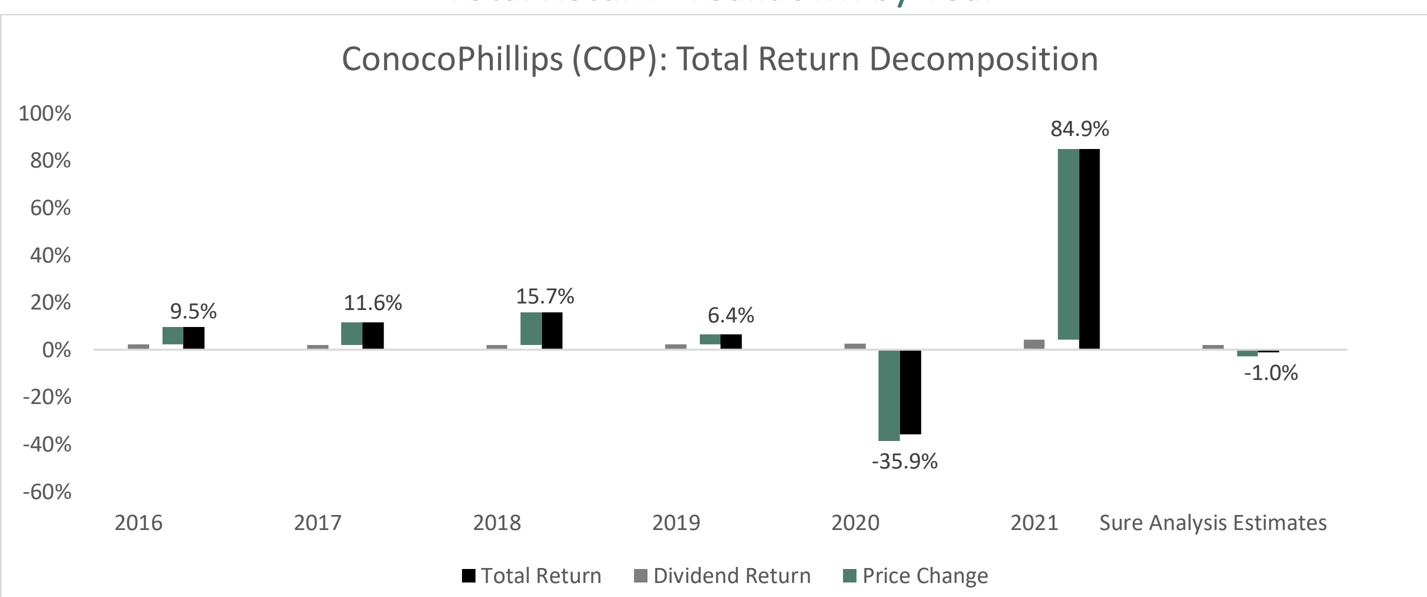
Since ConocoPhillips is a pure upstream company, it is much more leveraged to the price of oil than the well-known supermajors like Exxon Mobil and Chevron. Those companies remained profitable in the previous downturn of the energy sector (2014-2017) and avoided cutting their dividends. On the contrary, ConocoPhillips incurred heavy losses in 2015-2016 and cut its dividend by -66% in 2016. This unconvincing history, coupled with the high cyclicality of ConocoPhillips' business, makes us believe that the company is not a safe income stock.

ConocoPhillips has made questionable investments in the past, such as its drilling rights in the U.S. Arctic and its deep-water business in Senegal. However, the company seems to have learned its lesson and has become much more disciplined, investing only in high-return projects. Nevertheless, investors should be aware of the sensitivity of ConocoPhillips to the price of oil. During the last financial crisis, earnings-per-share plunged -70%.

Final Thoughts & Recommendation

ConocoPhillips is an oil and gas pure upstream play that is highly leveraged to the price of oil. Thanks to extremely tight global oil supply, ConocoPhillips is thriving right now. However, the stock has more than doubled in about 9 months and hence it could offer poor long-term returns. The stock could maintain its positive momentum in the short run, but we view it as unattractive from a long-term point of view. It thus receives a sell rating.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	57967	54413	52524	29564	23693	29106	36417	32567	18,784	45,828
Gross Profit	19362	17098	13187	1009	-1030	4613	10954	9313	841	14,768
Gross Margin	33.4%	31.4%	25.1%	3.4%	-4.3%	15.8%	30.1%	28.6%	4.5%	32.2%
SG&A Exp.	1106	854	735	953	723	561	401	556	430	719
Operating Profit	13,516	12,389	8,602	(4,957)	(3,932)	2,871	9,649	7,604	(1,554)	12,071
Op. Margin	23.3%	22.8%	16.4%	-16.8%	-16.6%	9.9%	26.5%	23.3%	-8.3%	26.3%
Net Profit	8,428	9,156	6,869	(4,428)	(3,615)	(855)	6,257	7,189	(2,701)	8,079
Net Margin	14.5%	16.8%	13.1%	-15.0%	-15.3%	-2.9%	17.2%	22.1%	-14.4%	17.6%
Free Cash Flow	(250)	604	(516)	(2,478)	(466)	2,486	6,184	4,468	87	11,672
Income Tax	7,942	6,409	3,583	(2,868)	(1,971)	(1,822)	3,668	2,267	(485)	4,633

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets ($B)	117.14	118.06	116.54	97.48	89.77	73.36	69.98	70.51	62.62	90.66
Cash & Equivalents	3618	6246	5062	2368	3610	6325	5915	5088	2,991	5,028
Acc. Receivable	9182	8487	6807	4514	3414	4320	4067	3401	2,754	6,670
Inventories	965	1194	1331	1124	1018	1060	1007	1026	1,002	1,208
Goodwill & Int.	---	---	---	---	---	---	---	---	---	---
Total Liabilities	68717	65565	64266	57402	54546	42561	37916	35,464	32,769	45,255
Accounts Payable	10013	9314	8026	4933	3653	4030	3895	3,200	2,698	5,025
Long-Term Debt	21725	21662	22565	24880	27275	19703	14968	14,895	15,369	19,934
Total Equity	47987	52090	51911	39762	34974	30607	31939	34,981	29,849	45,406
LTD/E Ratio	0.45	0.42	0.43	0.63	0.78	0.64	0.47	0.43	0.51	0.44

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	6.2%	7.8%	5.9%	-4.1%	-3.9%	-1.0%	8.7%	10.2%	-4.1%	10.5%
Return on Equity	14.9%	18.3%	13.2%	-9.7%	-9.7%	-2.6%	20.0%	21.5%	-8.3%	21.5%
ROIC	10.6%	12.7%	9.2%	-6.3%	-5.7%	-1.5%	12.8%	14.8%	-5.7%	14.6%
Shares Out.	1220	1230	1230	1240	1240	1180	1140	1100	1074	1321
Revenue/Share	46.26	43.89	42.16	23.81	19.02	23.84	30.98	28.99	17.42	34.51
FCF/Share	-0.20	0.49	-0.41	-2.00	-0.37	2.04	5.26	3.98	0.08	8.79

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