Imperial Oil (IMO)

Updated August 23rd, 2023 by Aristofanis Papadatos

Key Metrics

Current Price:	$56	**5 Year CAGR Estimate:**	0.2%	**Market Cap:**	$32.7 B
Fair Value Price:	$77	**5 Year Growth Estimate:**	-9.0%	**Ex-Dividend Date:**	8/31/2023
% Fair Value:	73%	**5 Year Valuation Multiple Estimate:**	6.6%	**Dividend Payment Date:**	10/1/2023
Dividend Yield:	2.6%	**5 Year Price Target**	$48	**Years Of Dividend Growth:**	8
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Rating:**	Sell

Overview & Current Events

Imperial Oil is one of Canada's largest integrated oil businesses. The company operates through three reporting segments: Upstream, Downstream, and Chemical. Imperial Oil is headquartered in Calgary, Alberta, Canada. Exxon Mobil (XOM) owns approximately 70% of Imperial Oil's common equity. Imperial Oil is cross listed on both the Toronto Stock Exchange and the New York Stock Exchange, where it trades with a market capitalization of $32.7 billion. Imperial Oil reports financial results in Canadian dollars, but the figures shown in this research report have been converted to U.S. dollars and refer to the company's NYSE-listed shares.

Imperial Oil is different from the well-known integrated oil majors, such as Exxon Mobil and Chevron, in one aspect. While the earnings of these companies greatly depend on the prices of WTI and Brent, the earnings of Imperial Oil are affected to a great extent by the prices of WTI and WCS (Western Canada Select). The latter usually trades at a deep discount to WTI, so it differentiates the earnings of Imperial Oil compared to those of the oil majors. In 2021 and 2022, the average discount of WCS to WTI was $13 and $18, respectively.

In late July, Imperial Oil reported (7/28/23) financial results for the second quarter of fiscal 2023. Production decreased -12% over the prior year's quarter due to planned turnaround activity. In addition, the price of oil and refining margins incurred a steep decrease off blowout levels, which had resulted from the sanctions of the U.S. and Europe on Russia. As a result, earnings-per-share plunged -68% over the prior year's quarter. Thanks to promising prospects at Kearl, we still expect Imperial Oil to grow its production this year. The company is likely to continue thriving in the near term thanks to above average oil prices but investors should be aware of the high sensitivity of the earnings of Imperial to the price of oil, which is highly cyclical.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$2.98	$3.30	$1.17	$0.56	$0.86	$2.20	$2.16	-$1.90	$2.74	$8.36	***$5.50***	***$3.43***
DPS	$0.46	$0.45	$0.39	$0.44	$0.50	$0.58	$0.64	$0.66	$0.82	$1.13	***$1.48***	***$1.84***
Shares[1]	847.6	847.6	847.6	847.6	831.2	790.0	749.9	734.1	689.5	603.0	***580.0***	***550.0***

Imperial Oil's earnings-per-share history has been volatile, largely due to the high volatility of oil prices, particularly during the 2014-2017 downturn, and the volatility of refining margins. Indeed, 2017 earnings-per-share were less than one-fourth of their peak levels. On the bright side, the energy market is currently recovering strongly from the pandemic. In addition, as Canada has the third-highest level of oil reserves worldwide, behind only Venezuela and Saudi Arabia, Imperial Oil has strong growth prospects in the long run. Furthermore, thanks to exceptionally high oil prices amid the war in Ukraine, Imperial Oil is thriving. Nevertheless, due to the cyclical nature of the oil industry, the price of oil is likely to deflate in the upcoming years. Due to the high comparison base formed by the expected earnings-per-share this year, we expect earnings-per-share to decline -9.0% per year on average over the next five years.

[1] 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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	14.1	14.4	31.5	---	35.6	13.9	12.4	---	10.4	5.7	***10.2***	***14.0***
Avg. Yld.	1.1%	0.9%	1.1%	1.4%	1.6%	1.9%	2.4%	3.9%	2.9%	2.4%	***2.6%***	***3.8%***

Imperial Oil is currently trading at a price-to-earnings ratio of 10.2, which is much lower than our assumed fair price-to-earnings ratio of 14.0. If the stock trades at our fair value estimate in five years, it will enjoy a 6.6% annualized gain thanks to the expansion of its valuation level.

Safety, Quality, Competitive Advantage, & Recession Resiliency

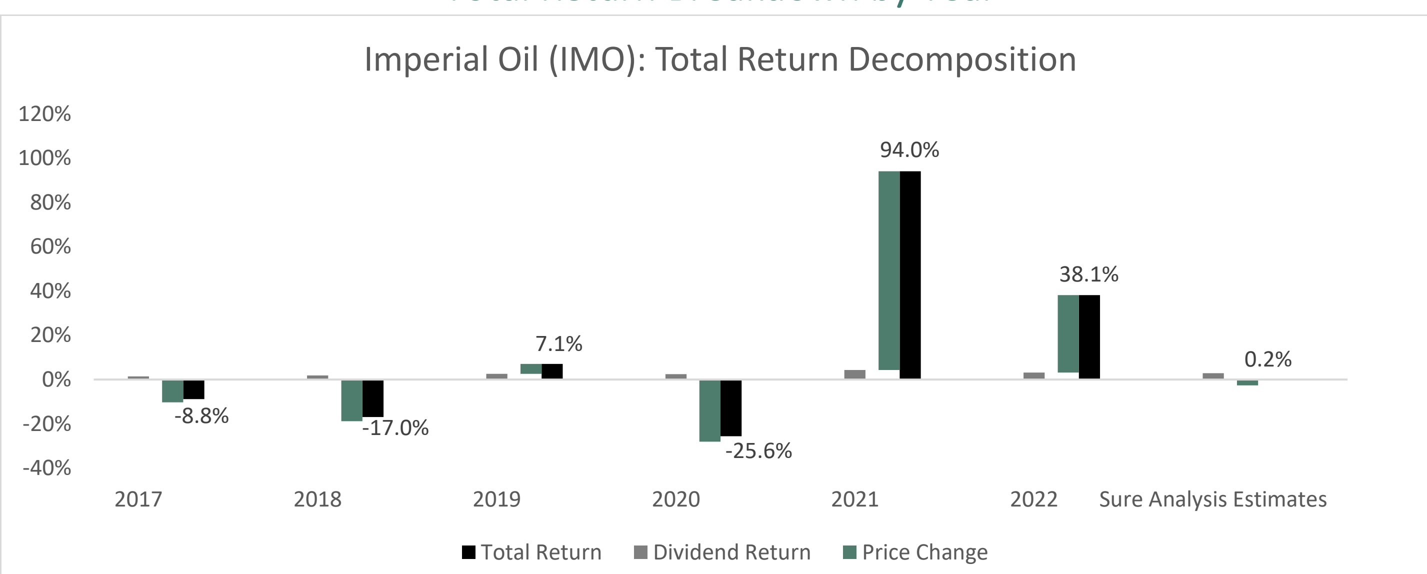
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	15.4%	13.6%	33.3%	78.6%	58.1%	26.4%	29.6%	---	29.9%	13.5%	***26.9%***	***53.5%***

Imperial Oil is one of the highest-quality energy businesses in the Canadian market. The company has a credit rating of AA+ from S&P, which is higher than all of its peers in the Canadian energy space. Moreover, the company has paid 100+ years of consecutive dividends and has increased its dividend (in Canadian dollars) for 27 consecutive years. The company's 10-year average dividend growth rate (again, in Canadian dollars) is 10%. Imperial Oil seems laser-focused on returning capital to shareholders. The company paid the same dividend for eight consecutive quarters due to the pandemic but it raised its dividend by 23% in 2021, by 26% last year and by 31% this year. Furthermore, the company benefits from leveraging the expertise of its major shareholder, Exxon Mobil.

Final Thoughts & Recommendation

Imperial Oil is thriving but we expect oil prices to deflate in the next few years, as producers will eventually grow their output at such high prices and sanctions on Russia may loosen. The stock of Imperial Oil has rallied 75% in the last 12 months and hence it has become risky from a long-term perspective. It may offer just a 0.2% average annual return over the next five years, as its 2.6% dividend and a 6.6% annualized valuation tailwind may be partly offset by a -9.0% annual decline of earnings-per-share. We maintain our sell rating. Even at lower stock prices, Imperial Oil is suitable only for investors who can tolerate the pronounced volatility that results from the dramatic swings of the price of oil.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	30,395	31,403	19,735	17,669	21,182	25,694	24,257	15,336	28,379	43,991
Gross Profit	4,609	4,920	2,366	1,167	1,195	3,148	2,358	(1,174)	3,281	7,833
Gross Margin	15.2%	15.7%	12.0%	6.6%	5.6%	12.3%	9.7%	-7.7%	11.6%	17.8%
SG&A Exp.	1,051	974	875	844	681	701	678	553	625	691
Operating Profit	3,439	3,886	1,434	252	373	2,433	1,645	(1,737)	2,630	7,138
Op. Margin	11.3%	12.4%	7.3%	1.4%	1.8%	9.5%	6.8%	-11.3%	9.3%	16.2%
Net Profit	2,746	3,428	879	1,635	378	1,786	1,658	(1,386)	1,977	5,642
Net Margin	9.0%	10.9%	4.5%	9.3%	1.8%	6.9%	6.8%	-9.0%	7.0%	12.8%
Free Cash Flow	(2,918)	(802)	(648)	711	1,366	1,876	2,104	(52)	3,484	6,884
Income Tax	883	1,120	628	211	71	586	(116)	(411)	641	1,648

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	34,954	35,172	31,109	30,895	33,082	30,437	32,296	29,824	31,985	32,069
Cash & Equivalents	255	185	146	290	950	725	1,315	605	1,689	2,762
Acc. Receivable	1,957	1,326	1,139	1,500	2,157	1,857	2,066	1,505	3,034	3,477
Inventories	1,289	1,293	1,163	1,051	1,193	1,349	1,464	1,438	1,405	1,671
Goodwill & Int.	262	242	161	138	148	137	142	130	130	122
Total Liabilities	16,618	15,764	14,229	12,337	13,651	12,457	13,712	13,028	14,939	15,555
Accounts Payable	4,243	3,419	2,154	2,368	3,083	2,708	3,261	2,473	4,066	4,564
Long-Term Debt	5,784	5,792	5,696	3,448	3,697	3,413	3,580	3,665	3,583	2,630
Total Equity	18,336	19,408	16,881	18,558	19,431	17,980	18,584	16,796	17,047	16,514
LTD/E Ratio	0.32	0.30	0.34	0.19	0.19	0.19	0.19	0.22	0.21	0.16

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	8.5%	9.8%	2.7%	5.3%	1.2%	5.6%	5.3%	-4.5%	6.4%	17.6%
Return on Equity	15.8%	18.2%	4.8%	9.2%	2.0%	9.5%	9.1%	-7.8%	11.7%	33.6%
ROIC	13.0%	13.9%	3.7%	7.3%	1.7%	8.0%	7.6%	-6.5%	9.6%	28.4%
Shares Out.	847.6	847.6	847.6	847.6	831.2	790.0	749.9	734.1	689.5	641.5
Revenue/Share	35.73	36.92	23.20	20.78	25.05	31.72	31.71	20.86	39.79	68.58
FCF/Share	(3.43)	(0.94)	(0.76)	0.84	1.61	2.32	2.75	(0.07)	4.89	10.73

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