



# Phillips 66 (PSX)

Updated February 1<sup>st</sup>, 2024 by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$144	<b>5 Year CAGR Estimate:</b>	-0.8%	<b>Market Cap:</b>	\$62.7 B
<b>Fair Value Price:</b>	\$150	<b>5 Year Growth Estimate:</b>	-5.0%	<b>Ex-Dividend Date<sup>1</sup>:</b>	2/16/2024
<b>% Fair Value:</b>	96%	<b>5 Year Valuation Multiple Estimate:</b>	0.8%	<b>Dividend Payment Date:</b>	2/28/2024
<b>Dividend Yield:</b>	2.9%	<b>5 Year Price Target</b>	\$116	<b>Years Of Dividend Growth:</b>	11
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	B	<b>Rating:</b>	Sell

## Overview & Current Events

Phillips 66 was spun off from ConocoPhillips in 2012. Phillips 66 has a market capitalization of \$62.7 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. In 2023, the refining segment was by far the most profitable segment, generating 49% of total earnings, as the sanctions of western countries on Russia resulted in extremely tight global supply of oil products and hence in sky-high refining margins.

In late January, Phillips 66 reported (1/31/24) financial results for the fourth quarter of fiscal 2023. Refining margins moderated sequentially, from \$18.96 to \$14.41 per barrel. As a result, the pre-tax income of the refining segment decreased from \$1.7 billion to \$0.8 billion and the adjusted earnings-per-share of the company declined -33%, from \$4.63 to \$3.09, though they exceeded the analysts' consensus by \$0.71.

On November 28<sup>th</sup>, 2023, activist investor Elliott Management announced the purchase of a \$1 billion stake in Phillips 66. Elliott Management also stated that it will seek two board seats and sees upside up to \$200 for the stock. Phillips 66 has rallied 22% since the announcement but we believe there is little upside left due to this development.

## Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
<b>EPS</b>	\$7.10	\$7.73	\$2.92	\$4.58	\$11.85	\$8.05	-\$0.89	\$5.70	\$18.79	\$15.81	<b>\$12.50</b>	<b>\$9.67</b>
<b>DPS</b>	\$1.89	\$2.18	\$2.45	\$2.73	\$3.10	\$3.50	\$3.60	\$3.62	\$3.83	\$4.20	<b>\$4.20</b>	<b>\$4.72</b>
<b>Shares<sup>2</sup></b>	571	547	530	519	464	441	439	441	466	430	<b>420</b>	<b>380</b>

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 in the positive phase of its cycle. While it has reduced its capital expenses in recent years, it has begun to reap the benefits from past investments.

The pandemic greatly affected the results of Phillips 66 in 2020 but the company has fully recovered from that crisis. Moreover, Phillips 66 has many ongoing growth projects in its midstream segment. Furthermore, it is thriving right now thanks to above average refining margins, which have resulted from the Ukrainian crisis. However, investors should be aware of the highly cyclical nature of refining margins. Given the exceptionally high earnings expected this year, we expect a -5.0% average annual decline of earnings-per-share over the next five years.

## Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
<b>Avg. P/E</b>	11.1	10.3	27.7	18.5	8.9	12.4	---	13.6	4.8	6.8	<b>11.5</b>	<b>12.0</b>
<b>Avg. Yld.</b>	2.4%	2.7%	3.0%	3.2%	2.9%	3.5%	5.3%	4.7%	4.2%	3.9%	<b>2.9%</b>	<b>4.1%</b>

<sup>1</sup> Estimated date.

<sup>2</sup> In millions.

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Phillips 66 is currently trading at a price-to-earnings ratio of 11.5. This valuation level is lower than its 10-year average of 12.7 of the stock. In order to be conservative, we assume a fair earnings multiple of 12.0 for this stock. If Phillips 66 trades at our fair value estimate in five years, it will enjoy a 0.8% annualized gain in its returns.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

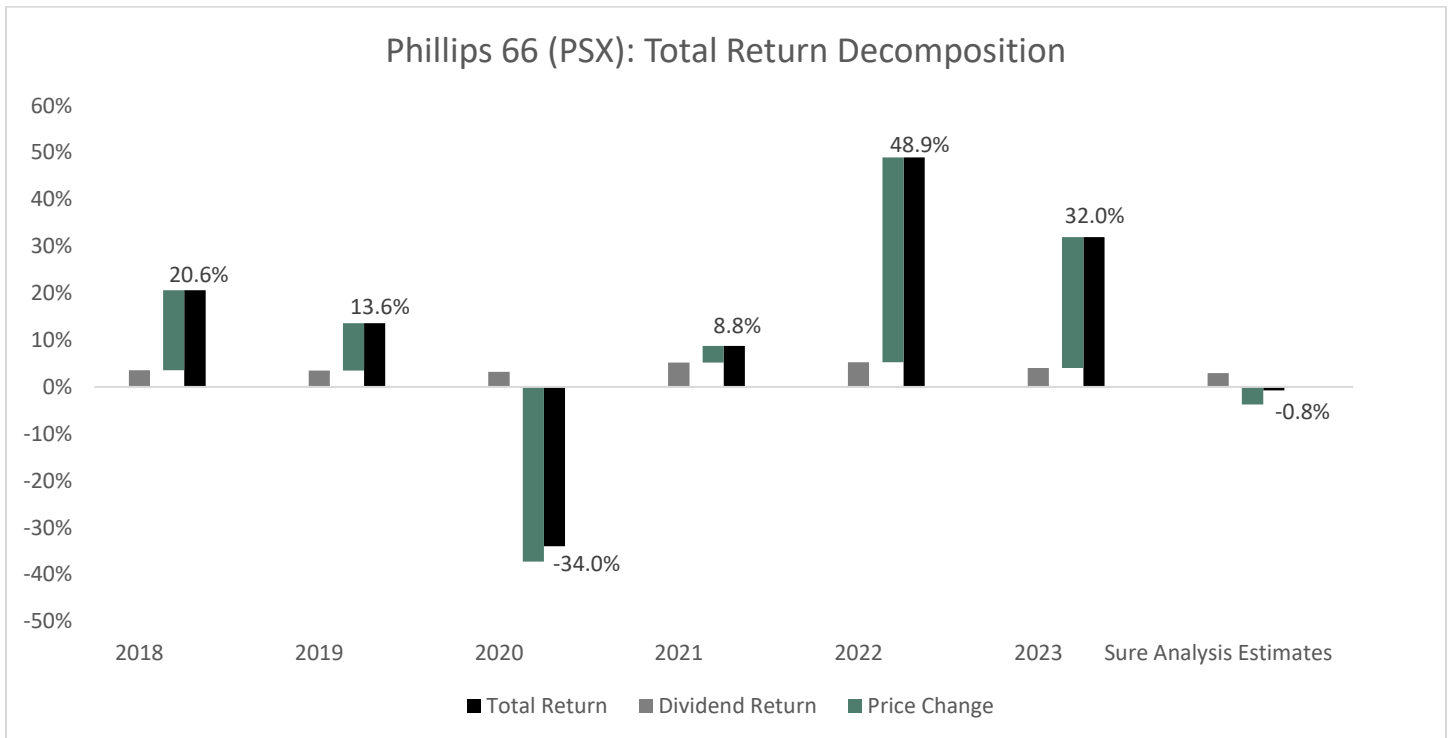
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	26.6%	28.2%	83.9%	59.6%	26.2%	43.5%	---	63.5%	20.4%	26.6%	33.6%	48.8%

Phillips 66 has a significant competitive advantage, namely the discipline of its management to invest only in high-return projects. Nevertheless, the company is cyclical, just like most oil companies. In the 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 downturn from the pandemic was much fiercer than the recent downturn and hence it forced Phillips 66 to post its first annual loss in its 10-year history. Nevertheless, the minor loss of -\$0.89 per share in 2020 is a testament to the diversified business model of Phillips 66 and its superior resilience to downturns when compared to its peers.

## Final Thoughts & Recommendation

Phillips 66 is a well-managed company, properly positioned for most scenarios of oil prices. However, the stock has more than doubled in about 28 months and hence it has become much less attractive. The latest part of the rally has been fueled by the purchase of a \$1 billion stake in the company by activist investor Elliott Management, which will also seek two board seats. Phillips 66 could offer a -0.8% average annual return over the next five years, as its 2.9% dividend and a 0.8% annualized valuation tailwind may be partly offset by a -5.0% annual decline of earnings-per-share. The stock receives a sell rating.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Revenue (\$B)</b>	161.2	99.0	84.3	102.4	111.4	107.3	64.1	111.5	170.0	147.4
<b>Gross Profit</b>	25,464	25,576	21,811	22,945	13,531	11,764	5,027	7,769	18,429	17,336
<b>Gross Margin</b>	15.8%	25.8%	25.9%	22.4%	12.1%	11.0%	7.8%	7.0%	10.8%	11.8%
<b>SG&amp;A Exp.</b>	1,663	1,670	1,638	1,695	1,677	1,681	1,544	1,744	2,168	2,525
<b>D&amp;A Exp.</b>	995	1,078	1,168	1,318	1,356	1,341	1,395	1,605	1,629	1,977
<b>Operating Profit</b>	3,430	4,548	1,098	1,838	5,209	3,335	(1,492)	468	9,620	7,950
<b>Op. Margin</b>	2.1%	4.6%	1.3%	1.8%	4.7%	3.1%	-2.3%	0.4%	5.7%	5.4%
<b>Net Profit</b>	4,762	4,227	1,555	5,106	5,595	3,076	(3,975)	1,315	11,024	7,015
<b>Net Margin</b>	3.0%	4.3%	1.8%	5.0%	5.0%	2.9%	-6.2%	1.2%	6.5%	4.8%
<b>Free Cash Flow</b>	(244)	(51)	119	1,816	4,934	935	(809)	4,157	8,619	4,611
<b>Income Tax</b>	1,654	1,764	547	(1,693)	1,572	801	(1,250)	146	3,248	2,230

## Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Total Assets</b>	48,692	48,580	51,653	54,371	54,302	58,720	54,721	55,594	76,442	---
<b>Cash &amp; Equivalents</b>	5,207	3,074	2,711	3,119	3,019	1,614	2,514	3,147	6,133	---
<b>Acc. Receivable</b>	7,255	5,173	6,397	7,506	6,173	8,510	6,522	7,470	10,985	---
<b>Inventories</b>	3,397	3,477	3,150	3,395	3,543	3,776	3,893	3,394	3,276	---
<b>Goodwill &amp; Int.</b>	4,174	4,181	4,158	4,146	4,139	4,139	2,268	2,297	2,317	---
<b>Total Liabilities</b>	26,655	24,642	27,928	26,943	27,149	31,551	33,198	33,957	42,336	---
<b>Accounts Payable</b>	8,064	5,655	7,061	8,027	6,586	8,575	5,549	8,461	11,323	---
<b>Long-Term Debt</b>	8,635	8,887	10,138	10,110	11,160	11,763	15,629	14,158	17,190	---
<b>Total Equity</b>	21,590	23,100	22,390	25,085	24,653	24,910	18,984	19,166	29,494	---
<b>D/E Ratio</b>	0.40	0.38	0.45	0.40	0.45	0.47	0.82	0.74	0.58	---

## Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Return on Assets</b>	9.7%	8.7%	3.1%	9.6%	10.3%	5.4%	-7.0%	2.4%	16.7%	---
<b>Return on Equity</b>	21.9%	18.9%	6.8%	21.5%	22.5%	12.4%	-18.1%	6.9%	45.3%	---
<b>ROIC</b>	16.1%	13.3%	4.7%	14.3%	14.8%	8.0%	-10.5%	3.6%	25.2%	---
<b>Shares Out.</b>	571	547	530	519	464	441	439	441	474	453
<b>Revenue/Share</b>	282.08	180.95	159.00	197.40	235.13	236.39	145.90	253.15	358.83	325.23
<b>FCF/Share</b>	(0.43)	(0.09)	0.22	3.50	10.41	2.06	(1.84)	9.44	18.19	10.17

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

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