The Henry Fund
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MARATHON PETROLEUM CORPORATION (MPC)

November 9, 2022

Energy – Oil and Gas Refining and Marketing

Stock Rating **BUY**

Investment Thesis

We have a **BUY** rating on Marathon Petroleum Corporation (MPC). MPC shares are currently trading at $120 per share, which is well below our target range of $135 to $140 with an upside of 15.06%. We understand the risks associated with volatile communities, such as gas and oil. For the sake of our fund's performance, it is imperative that we have exposure to gas and oil, due to the Henry Fund Consensus' bearish mid-term to long-term economic outlook of these commodities. Furthermore, we believe MPC is a natural pairing with current HF holding ConocoPhillips (COP) to give a flexible integrated-esque exposure to the fund.[1]

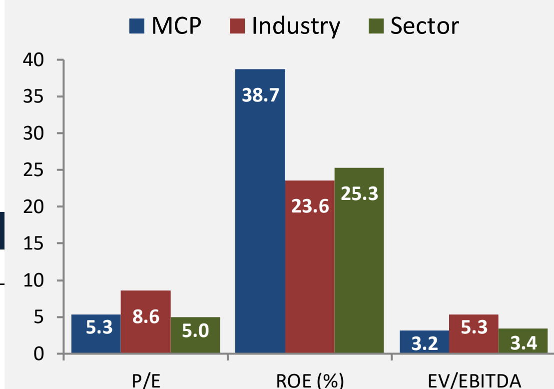
Drivers of Thesis

- With global supply at near-term lows, as a result of the Russia-Ukraine conflict, demands continues to push toward levels experienced in 2019.
- MPC has a clear and evident history of returning capital to stockholders. In Q3, they announced completions of a $15 billion return of capital, repurchase of 30% of shares outstanding.
- Marathon Petroleum has above-average refining complexity, permitting MPC to process more lower-cost heavy and sour crudes (To allow for better margins relative to peers).

Risks to Thesis

- A potential shock to demand of gas and oil to due federal regulations or major economic decline could result in catastrophic impact on firm's heath.
- The recent spinoff of Speedway retail has manufactured higher dependence on refining, where margins are often volatile.
- MPC lacks deep geographic diversity with zero refineries located internationally.

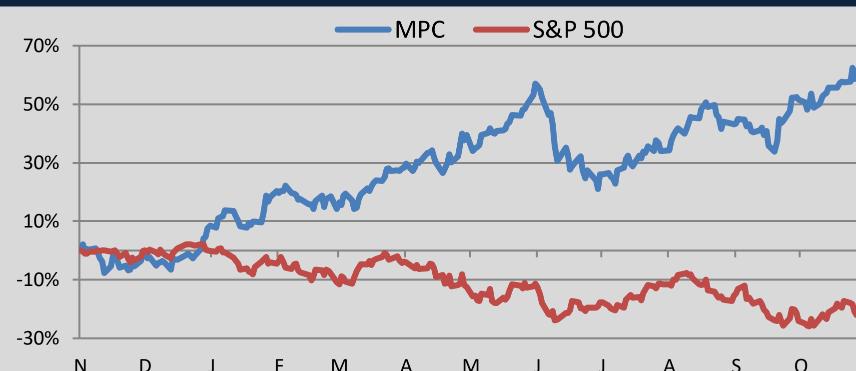
Target Price	$135-140
Henry Fund DCF	$133
Henry Fund DDM	$175
Relative Multiple	$144
Price Data	
Current Price	$120
52wk Range	$60 – 121
Consensus 1yr Target	$131
Key Statistics	
Market Cap (M)	$56,005
Shares Outstanding (M)	$488.7
Institutional Ownership	79.4%
Beta	0.95
Dividend Yield	2.5%
Est. 5yr Growth	11.01%
Price/Earnings (TTM)	5.3
Price/Earnings (FY1)	23.8
Price/Sales (TTM)	0.37
Price/Sales (FY1)	0.40
Profitability	
Operating Margin	10.0%
Profit Margin	7.42%
Return on Assets (TTM)	11.73%
Return on Equity (TTM)	38.76%



Earnings Estimates

Year	2019	2020	2021	2022E	2023E	2024E
EPS	$4.94	-$3.44	$2.45	$25.23	$13.72	$9.60
HF est.				$27.78	$17.58	$14.86
Growth	*-22.08%*	*-169.64%*	*-171.22%*	*1,033.8%*	*-36.71%*	*-15.45%*

12 Month Performance



Company Description

Marathon Petroleum Corporation (MPC) operates in the refining, marketing, and transportation of petroleum products nationally across the United States. MPC is an independent firm, which manages the nation's largest refining system with a 2.9 million barrels per day of crude oil refining capacity. Its' business segments include Refining & Marketing and Midstream. Its headquarters are located in Findlay, Ohio.[1]

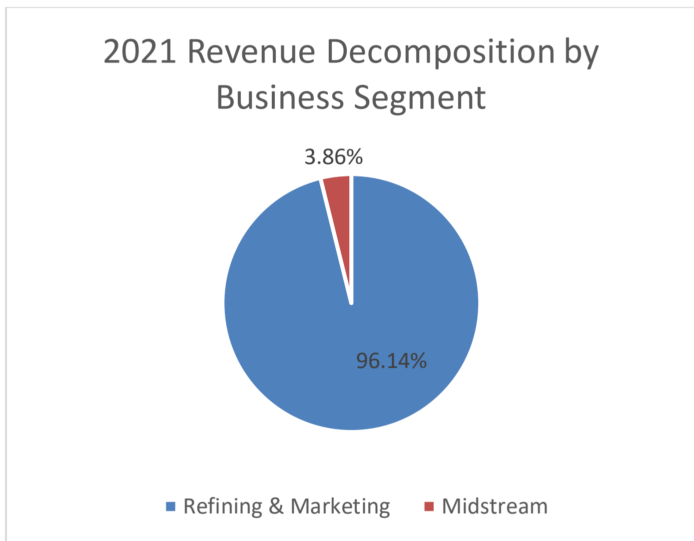
Important disclosures appear on the last page of this report.

COMPANY DESCRIPTION

On June 30, 2011, Marathon Oil Corporation (MRO) spun off its downstream business. This created a new independent refining company, Marathon Petroleum Corporation (MPC). MPC operates and owns 16 refineries, all located in the United States. MPC has three marketing areas: Gulf Coast, Midwest, and West. Marathon's midstream operates are primarily managed through MPLX LP (MPLX 28 NR), which MPC owns a 62% stake. MPLX LP operates and owns crude oil and light product logistics and transportation infrastructure, as well as processing, fractionation, and gathering assets.[6]

Its headquarters are located in Findlay, Ohio. MPC manages the nation's largest refining system with a 2.9 million barrels per day of crude oil refining capacity. At FYE 2021, MPC had approximately 17,700 employees across full time and part time roles (roughly 3,600 employees are covered by a collective bargaining agreement).

Marathon Petroleum Corp. is amongst the largest US wholesale suppliers of gasoline and distillates to resellers. MPC hosts a massive integrated midstream asset network, which links producers of NGLs and natural gas from many of the major US basins to both national and international markets. MPC has two business segments: Refining & Marketing and Midstream. Each of these segments are organized and managed on the nature of its product and services offerings.



Source: MPC 2021 10K

Marathon Petroleum Corporation is a pure play refinery firm with over 96% of their 2021 revenue arriving from its Refining & Marketing segment. Marathon Petroleum Corporation does not directly face any currency risk, as 100% of its revenue is from United States based operations.

Refining & Marketing

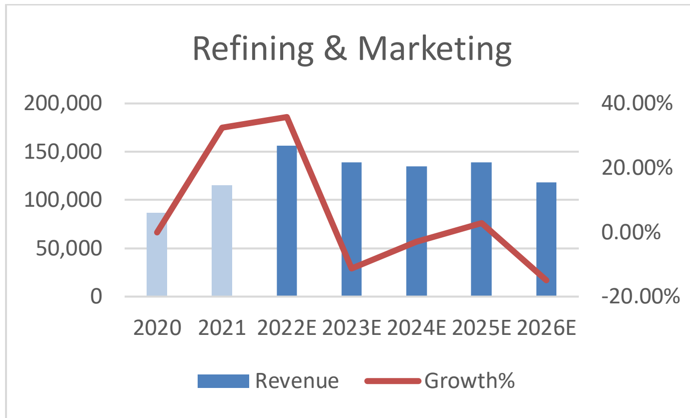
The Refining & Marketing segment includes the operation and ownership of MPC's 16 refineries. Collectively these refineries have a refining capacity 2,874,000 BD as of February 2021 and are located throughout the West, Midwest, and Gulf Coast of the United States.

MPC Refining Operations Map

Source: Marathonpetroleum.com

This segment refines crude oil and other feedstocks at the refineries nationally and purchases refined products (including renewable diesel) and ethanol to resell and distribute. The transportation, storage, marketing, and distribution is primarily provided by the midstream segment. The end market for its products includes buyers of spot prices, independent entrepreneurs (who operate Marathon branded outlets), international and domestic wholesale marketing customers, and long-term supply contracts to retailers under the ARCO brand.[4 & 19]

In October 2018, MPC significantly increased its capacity thanks to the Andeavor deal, which added 1,117,000 BD of capacity and 10 refineries. During the FY 2020, Marathon's refineries processed 2,418,000 BD of crude oil (84% utilization) and had 165,000 BD of blendstocks and other charges. The extremely low utilization of 84% is a result of the COVID-19 pandemic. In the FY 2019, MPC recorded a utilization of 95%. Its refining capacity is allocated as approximately 40% in the Midwest, 19% in the West, and 41% in the Gulf Coast.



Source: Henry Fund Model & FactSet

We expect the Refining & Marketing segment to have a strong finish to the FYE 2022 with an expect YoY growth of 35.79%. Thereafter, we expect the crack spread to revert toward the historical levels that predated COVID-19 and Russia-Ukraine situation. For the forecasted years, 2022E-2025E we used the 12-month CME Group futures price for crack spread. For the terminal year, we used the 2026E 12-month futures crack spread times the 2020 crack spread. This assimilates the new "normal" post-COVID-19 and the Russia-Ukraine situation. The largest difference for our forecast versus the consensus estimates is that we believe the crack spread will continue to be at high levels for our terminal year.

Midstream

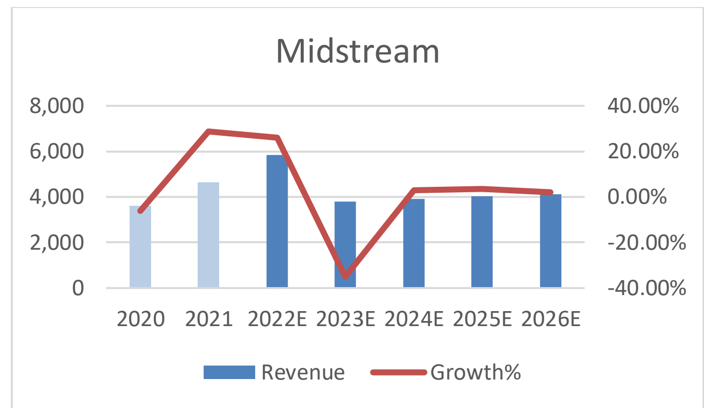
The Midstream segment includes the refined products pipelines and crude oil pipelines. In 2020, had an aggregated refined products pipelines and crude oil pipeline throughput of 5.2 MMBD, natural gas processed of 8.44 BCFE, and NGL processed of 370,000 BD. [19]

MPC Midstream Operations Map

Source: Marathonpetroleum.com

The former Retail segment has been reclassified as "held for sale". Held for sale pertains to the sales of gasoline and merchandise through retail outlets owned and operated by the segment. These retail outlets are primarily under the Speedway brand, in seven Midwest states.

At FYE 2020, MPC owned roughly 3,800 retail stores (1,100 acquired in Andeavor deal). In August 2020, MPC agreed to its Speedway business to 7-Eleven in a $21 billion all-cash deal. In May 2021, the 7-Eleven deal closed and 7-Eleven agreed to a 15-year deal to source its fuel from Marathon.



Source: Henry Fund Model & FactSet

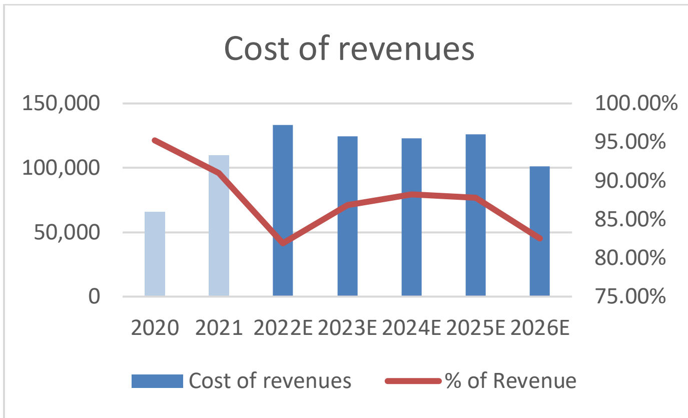
We expect the Midstream segment to have a 28.73% YoY growth. We then have the segment revert back to historical levels to as we expect the supply shock to be resolved in the near-term.

Cost Structure Analysis

MPC has two major operating expenses, Cost of revenue and Selling; general and administrative Expense.

Cost of Revenue

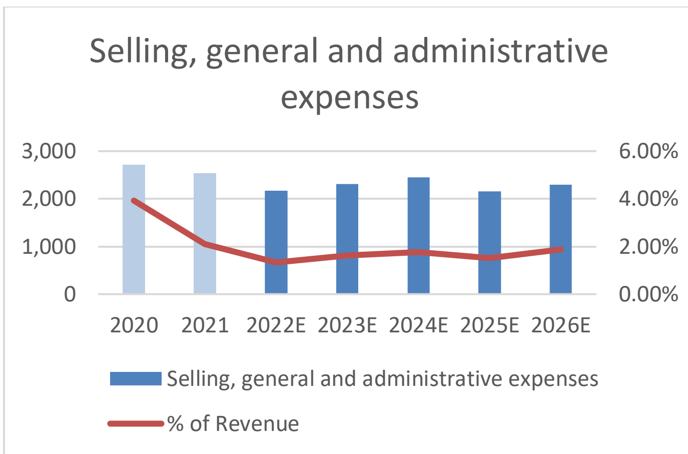
Cost of Revenue is largely determined by demand of product and commodity costs. We see input costs continuing rising up until the terminal year to keep up with inflation. We used the historical variable cost (difference in the Refining & Marketing margin and crack spread) times Refinery throughputs (mbpd) of products times plus the historical fixed cost with association to production. We believe the fixed cost will be lower in the terminal as production could be slightly lower in an energy transition We do not expect this for in the near-term.



Source: Henry Fund Model & FactSet

Selling, general, and administrative expense

Selling, General and Administrative includes marketing expenses, professional fees, technology related costs, etc. We see project these costs to stay within historical averages with revenue for the foreseeable future. We used the four-year historical average SGA to get the SGA as a percent of sales. We used this percentage of sales for the forecasted period.



Source: Henry Fund Model & FactSet

Debt Maturity Analysis

Marathon's has a S&P credit rating of BBB with a stable outlook. Using the Standard & Poor's credit rating scale bonds, those who have a rating of BBB- or better are considered "investment grade." This is ideal because having a better rating allows more asset managers' charters to allow for trading on the market. [1]

Fiscal Year	Payment ($mil)
2022	500
2023	1,500
2024	2,201
2025	2,950
2026	2,249
Thereafter	15,568
Total	24,968

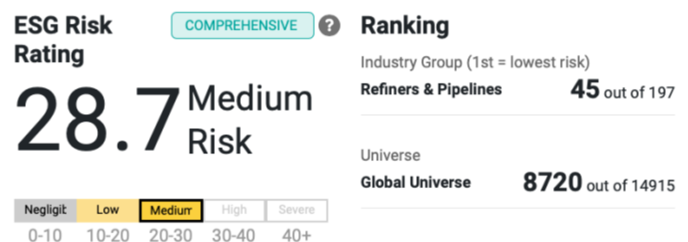
Source: MPC 2021 10K

Over 60% of MPC's debt is due past five years allowing Marathon to operate organically, without urgency of solvency issues.

Per management guidance, MPC is planning on maintaining its current credit profile. Due to the current economic climate, MPC in the near-term will have the option to pay down its debt earlier and reduce its levered position. However, due to rising interest rates it is optimal to keep debt outstanding and give surplus capital back to shareholders in the form of dividends and share buybacks.

ESG Analysis

ESG stands for environmental (E), social (S), and corporate governance (G). The Risk Rating below was rated by Morningstar's Sustainalytics.



Source: Sustainalytics

Sustainalytics calculates firms' ESG Risk Ratings by measuring firms' exposure and management risk, as well as its controversy rating. Marathon had high exposure risk, strong management of material risk, and three out of five controversy rating. We believe MPC had a high exposure risk do its business model of refining carbon-based products.

Marathon had strong management of material risk due to its practices and policies aligning with its sub-industry, in large part regarding environmentally conscience decision

making. MPC had its highest controversy rating of three of five which was because of community relations issues.

Despite Marathon's business model being built around carbon products and services. MPC has a relatively high ESG rating due to its commitment to occupational health and safety, as well as strongly perceived corporate governance.[21]

RECENT DEVELOPMENTS

Marathon Q3 Earnings

On November 1st, 2022, Marathon Petroleum Corp. reported its third quarter EPS at $7.81, which beat consensus estimates of $7.09. Out of the last five quarter, MPC has beaten consensus estimates four times. The reason for beating the market estimates was improvements and execution of its refining system, as it was near full utilization to meet demand.

MPLX is increasing its distribution by 10%, which will lead to an expected $2 billion collection for MPC on an annual basis. MPC has announced its completion of $15 billion return of capital commitment, from the proceeds of the Speedway divestiture; MPC has repurchased 30% of shares outstanding. Marathon announced it is increasing its dividend to $0.75 per share, which is approximately a 30% increase.

Russia Exposure

Marathon Petroleum Corporation does not conduct business in or with Russia. However, the Russia-Ukraine conflict and aftermath's externalities will have a direct impact on both supply and demand of gas and oil to every corner of the world.

CORPORATE ACTIONS

Speedway Sale

On May 2021, MPC completed the sale of Speedway to 7-Eleven, Incorporated for cash proceeds of $21.38 billion. Speedway was a firm-owned and operated retail fuel and convenience store. This transaction resulted in MPC gaining $11.68 billion pretax. MPC has committed these net proceeds to strength its balance sheet and return capital to shareholders.

Andeavor Acquisition

On October 2018, MPC acquired Andeavor. Andeavor shareholders received in aggregate roughly 240 million shares of MPC common stock valued at $19.8 billion and $3.5 billion in cash. Andeavor was a highly integrated logistics, marketing, and refinery firm that operating in the west and midwest United States. This acquisition substantially increased the geographic diversification and scale of MPC's assets. This also allowed for opportunities to better utilize and optimize previously owned assets within its system.

INDUSTRY TRENDS

Midstream Moving Toward to Renewables?

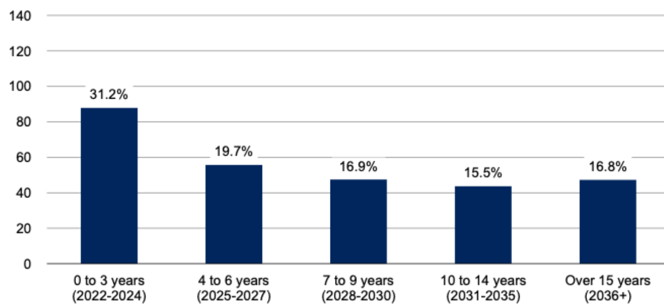
Midstream firms are diversifying their businesses to include renewable energy, like wind, solar, geothermal, etc. As ESG concerns mount from shareholders, midstream firms have listened and implemented their at least part of desires. It is also a way to build an alternative long-term future outside of fossil fuel and in some cases reduce costs.

Midstream firms can be energy intensive, as liquid pipelines can transport product vastly across the continent, if needed. As a renewable power has become increasingly cheaper over recent history, especially relative to fossil fuels, which are trending upward in cost.

Enbridge was the first midstream firm to invest in a wind firm in 2002. Since then, it has built similar projects in several Europe countries and in Canada. The Williams Companies have recently committed to becoming a net zero emitter by 2050.

End of Long-Term Natural Gas Contracts?

Historically, natural gas pipeline contacts for midstream firms are long duration, often 15 to 25 years. However, recent data suggest that contracts as of lately have been shifting toward much shorter durations with more flexible commercial terms. It is estimated that approximately 50% of the total natural gas pipeline contracts will be expire in the next six years, as shown by the figure below:



Source: S&P Global Market Intelligence

With more uncertainly raised by a lack of a long-term contracts, this could result in less capital spending by this sub-industry.

MARKETS AND COMPETITION

Threat of New Entrants

The threat of new entrants is **low**. The barrier of entry is extremely high due to the capital-intensive and highly regulated nature of the industry. For a new entrant to establish themselves as a viable competitor, they would have to have high upfront capital investments in R&D and infrastructure. That new entrant would also have to deal with state and environmental regulations, in addition to approval for pipelines by the Federal Energy Regulatory Commission (FERC).[16 & 1]

Threat of Substitutes

The threat of substitutes is **low**. There are alternatives to using pipelines, as oil and natural gas can be transported by rail, truck, or boat. Natural gas needs to change forms into NGLs in these scenarios. As a gas, it must be compressed and move by pipeline. Nevertheless, pipelines are main transportation method for gas and oil due to it being the cheapest option. Transportation by pipeline is approximately ten times cheaper than by truck, barring bottleneck, which cause pipeline transportation rates to be hiked. [16 & 1]

Intensity of Competitor Rivalry

The intensity of competitor is **high**. Appalachia, Permian, Bakken, and Eagle Ford basins are served by major midstream firms. Pipelines and other logistics infrastructure operated by larger midstream firms are usually longer (In some cases interstate) and have larger capacity. Oil & gas producers and midstream firms generally sign long-term contacts (15 to 25 years), typically negotiation for transportation rates are based off of deliverable volumes of product. During periods of low utilization competition intensifies; midstream firms will offer bountiful discounts to garner the business of producers.

Bargaining Powers of Customers

The bargaining power of customers is **moderate**. In 2018 and 2019, the Appalachia; Bakken; and Permian regions were hit with major capacity constraints. This resulted in too many producers chasing too little capacity; which caused the customer to have less bargaining power. The midstream industry adapted and added capacity near the end of 2019.

However, the US is forecasted to cross record levels of production by 2023. With ESG pressure to slow down the industry and higher production could result in scarcity in major regions, especially in the Permian Basin. [16 & 1]

Bargaining Powers of Suppliers

The bargaining power of suppliers is **low** and is trending toward, at least in the near-term. The launch of several new pipelines in the first of 2020, brought a large quantity of options and flexibility for markets and consumers, who were previously starving for options. As pipeline are built out producers will find a way to utilize these to capacity, at least incremental capacity. Obviously, unless a major macroeconomic shock (i.e., global pandemic) comes into play, which we do not foresee in the near term. [16 & 1]

Porter's Five Forces Summary

Overall, we have a positive outlook on the Oil and Gas Refining and Marketing Sub-Industry. This sub-industry has been and will continue to benefit in the foreseeable future from geopolitical tensions between Ukraine and Russia. Obviously, this is a volatile industry with high, highs and low, lows. In early 2022 demand for fined products was high allowing $60 per barrel range, generally it is between $10-$20. The industry is highly

concentrated and not appealing for new entrants because of a potential for an energy transition and capital intensity required. The high margin is near-term phenomena and is a market correction for demand during COVID-19.

As long as there is not major government interference and, or a major technological advancement in the EV space. This is sub-industry will be healthy and profitable. This is a sub-industry with high volatility, we understand that and have a bullish outlook both near and long-term relative to Wallstreet. [16 & 1]

PEER COMPARISONS

The Oil and Gas Refining and Marketing Sub-Industry is where raw materials (i.e., crude oil or natural gas) are processed into refined products (i.e., gasoline, jet fuel, etc.). The end-markets for these products include airlines, buyers of spot prices, independent entrepreneurs, and many more. The companies we compared are Occidental Petroleum Corporation (OXY), HF Sinclair Corporation (DINO), Philips 66 Company (PSX), Valero Energy Corporation (VLO), Delek US Holdings, Inc (DK), and Par Pacific Holdings, Inc. (PARR).

Occidental Petroleum Corporation (OXY)

Occidental Petroleum Corp. focuses on the exploration and production of oil and natural gas, as well as downstream and midstream operations. Its business segments operations are the following: Oil & Gas (70%), Chemical (19.4%), and Midstream & Marketing (10.6%). OXY was founded in 1920 and is headquartered in Houston, Texas. OXY is one of the largest gas and oil companies in the United States. This firm as far as E&P of Gas and oil is more involved in midstream oil than the rest of their industry. [7]

HF Sinclair Corporation (DINO)

HF Sinclair Corp. focuses on the processing and marketing of transportation fuels and associated products. Its business segments operations are the following: Refining (85.6%), Lubricants & Specialty Products (13.9%), and Holly Energy Partners (0.6%). HF Sinclair Corp. was incorporated in 2021 and is headquartered in Dallas, Texas. DINO owns 6 refineries amongst the Midwest and western United States. In addition, HF Sinclair supplies over 1,300 independent Sinclair-branded gas stations. This firm produces and markets gasoline, renewable diesel, diesel fuel, jet fuel, and other associated products.

Phillips 66 (PSX)

Phillips 66 focuses on the processing, storage, and marketing of transportation fuels and associated products. Its business segments operations are the following: Marketing & Specialties (66.3%), Refining (25.7%), Midstream (7.9%), and Chemicals (0.1%). PSX was founded in 1875 and is headquartered in Houston, Texas. It was spun off from ConocoPhillips in 2012, creating an independent downstream energy company. Phillips 66 owns 13 refineries, that possess a net crude oil capacity of 2.2 million barrels per day; approximately 22,000 miles of pipeline systems; roughly 7,500 branded marketing outlets; and 6.7 billion cubic feet per day of natural gas capacity.[9]

Valero Energy Corporation (VLO)

Valero Energy Corp. focuses on the processing and marketing of transportation fuels and associated petrochemical products. Its business segments operations are the following: Refining (93.8%), Ethanol (4.5%), and Renewable Diesel (1.6%). Valero Energy was founded in 1980 and is headquartered in San Antonio, Texas. VLO is the world's largest independent petroleum marketer and refiner in the world with most of its sales from the United States, Canada, and the United Kingdom. Its product selection includes conventional gasoline, jet fuel, asphalt, and other associated refinery products. At the FYE 2021, VLO operated and owned 14 refineries with an aggregated throughput capacity of 3.15 million barrels per day.[10]

Delek US Holdings, Inc. (DK)

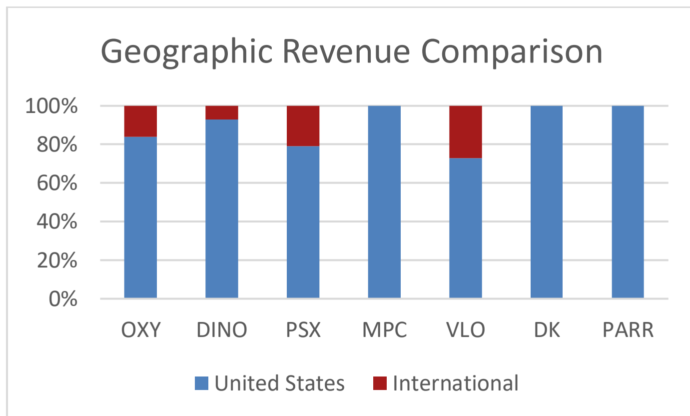
Delek US Holdings, Inc. focuses on the logistics and marketing of crude oil, as well petroleum refining. Its business segments operations are the following: Refining (89.5%), Retail (7.8%), and Logistics (2.8%). DK was founded in 2001 and is headquartered Brentwood, Tennessee. Delek US Holdings operates and owns four

refineries and three biodiesel facilities. DK owns and leases storage tanks for associated crude oil with a capacity of 10.2 million barrels, roughly 400 miles of crude oil transportation pipelines, roughly 450 miles of refined product pipelines, as well as a 900-mile crude oil gathering system. The retail segment owns and leases 248 convenience stores, that offer various gasoline and associated products in mostly western Texas and New Mexico.[24]

Par Pacific Holdings, Inc. (PARR)

Par Pacific Holdings, Inc. focuses on the performance of energy through oil refining and infrastructure businesses. Its business segments operations are the following: Refining (87.5%), Retail (8.9%), and Logistics (3.6%). PARR was founded in 1984 and is headquartered Houston, Texas. Par Pacific Holdings, Inc. changed its name in 2015 from Par Petroleum Corporation. PARR operates three refineries that produce gasoline, ultra-low sulfur diesel, jet fuel, asphalt, and other associated products. The consumption of its products are mostly in the northwest United States and Hawaii. The retail segment includes operation of 119 fuel retail outlets.[11]

Oil and Gas Refining and Marketing Sub-Industry Geographic Comparison



Source: FactSet

As the United States' dollar strengths relative to other major currency. It is ideal for firms conducting business in domestic markets. MPC, DK, and PARR all had no exposure to foreign markets. While VLO had the most exposure to foreign markets as only 73% of its revenue is from the United States and the remaining portion was mostly Canada and the United Kingdom.

Oil and Gas Refining and Marketing Sub-Industry Debt Comparison

TCKR	LT Debt/Assets	EBITDA/Interest Expense	Debt Rating
MPC	30.3	5.9	BBB
OXY	38.3	8.2	BB+
DINO	26.1	9.5	BBB-
PSX	24.6	4.9	BBB+
VLO	23.1	7.8	BBB
DK	33.9	1.0	BB-
PARR	34.9	1.7	NR

Source: FactSet

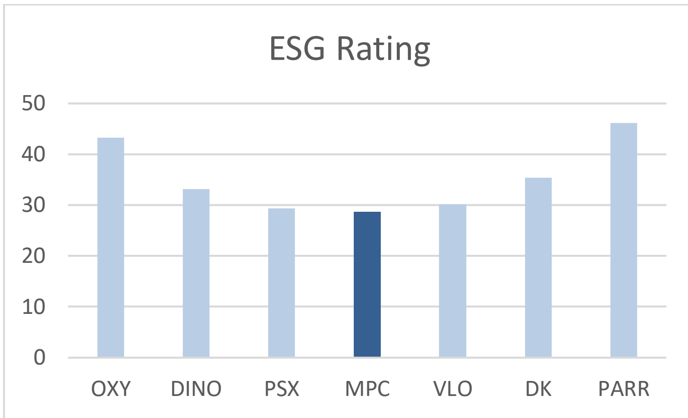
The chart above compares the Oil and Gas Refining and Marketing Sub-Industry firms' debt and credit rating (S&P). We believe it is likely that interest rates rise significantly in the near-term. If there is a demand shock, firms with less levered positions, relative to their EBITDA and total assets, will have drastically more flexibility in this economic climate.

Occidental Petroleum has the worst long-term debt to assets ratio. However, OXY has a high concertation in Oil and Gas exploration and production. This could be major factor in being the largest negative outlier. The best long-term debt to assets ratio despite business segments in high capital-intensive segments, such as ethanol and renewable diesel.

With the EBITDA to interest expense ratio, the higher the ratio, the better financial durability the firm has. Sinclair had the best ratio due to its pre-tax income relative to its interest expense, which is high for its industry because of its poor credit rating. DK had the worst at 1.0. Certainly, Delek's debt situation faces the highest risk for liquidity issues upon a shock in demand of oil and gas.[1]

ESG Comparison Analysis

ESG stands for environmental (E), social (S), and corporate governance (G). The Risk Ratings below were rated by Morningstar's Sustainalytics.



Source: Sustainalytics

The chart above compares each Oil and Gas Refining and Marketing Sub-Industry firms' ESG Rating. The lower the score the better, rating are between 0 and 50.

PARR was the most notable of this sub-industry, due to its serve ESG risk (46.1). This risk is because of the carbon emissions and waste externalities that this firm produces. OXY is within comparable serve ESG risk (43.3), but has a diverse set of issues, such as poor business ethics, carbon emissions, poor business relations, and more. MPC had the best ESG risk in the sub-industry because of its focused corporate governance toward ESG issues.[21]

ECONOMIC OUTLOOK

Federal Interest Rates

The federal funds rate as shown below has been drastically increased in 2022. The last four fed meetings have results in 75 bps rises in an attempt to stop inflation, which thus far seem unsuccessful. We believe the federal reserve will continue to raise rates to around 5% before slowing down the rate hikes.

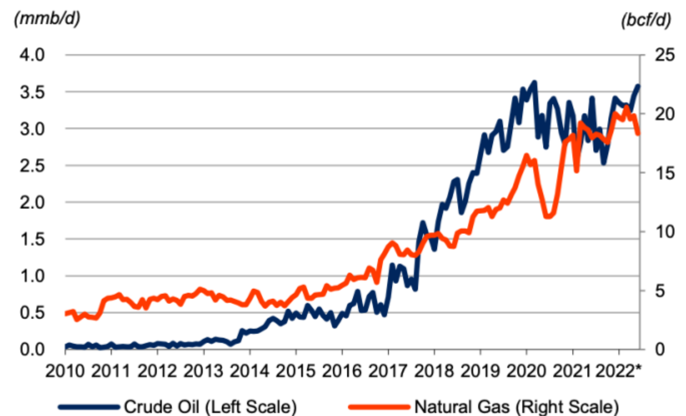
This industry is highly dependent on debt as it is needed for heavy capital expenditures and acquisitions. The rates will certainly make firms less active in corporate activity and responsible firms will lower their levered positions.

Fed Funds Rate

Source: TradingEconomics

U.S. Exports of Crude Oil & Natural Gas

As shown in the chart below, the United States is generally trending upward for exports of both crude oil and natural gas as result of a multitude of factors. Most notably European Union regulations are more strict than the United States and Europeans are more ESG conscience than the Americans. [14]



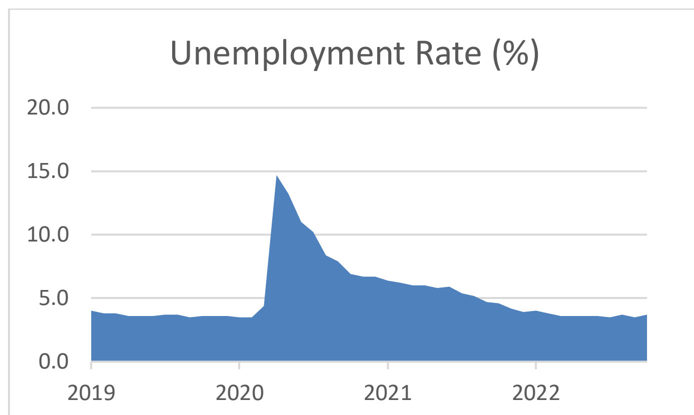
Source: U.S. Energy Information Administration

The United States will more than likely see exports at near-term high until the conclusion of the Ukraine-Russia conflict. Even after, the United States still could see comparable demand due to the Europeans refusal to support Russia's economy.[13]

US Unemployment Rates

The unemployment rate is the percentage of the participating labor force who are currently unemployed. It is commonly used as a lagging indicator of changing

economic conditions, rather than a predicating indicator of changing economic conditions. We see this as a principal factor for energy consumption, as most people use vehicles to get to their workplace. As long as unemployment is relatively low (3-4%), there will be a high demand for energy. We expect this number to rise in the next 5-10 years. It will be a lagging factor that we are in a recession and that the demand for energy is down within correlation.



Source: Fred

As shown above, the United States unemployment rate is 3.7%, which is relatively strong. We believe it will continue to be stable in the near term barring a major shock (i.e., COVID-19).[2]

VALUATION

Revenue Decomposition

The relative valuation uses peers' financial ratios that have similarities to the target company to arrive at an implied relative value. We selected Occidental Petroleum Corporation, HF Sinclair Corporation, Philips 66 Company, Valero Energy Corporation, Delek US Holdings, Inc., and Par Pacific Holdings, Inc. as peers for the Oil and Gas Refinery & Marketing Sub-Industry. The financial metrics used were 2023E P/S, and 2024E P/S. After getting the peers' average for each metric it is used as a multiple to arrive at the implied relative value. We multiplied the Marathon's financials metrics times the peers' multiples and averaged these out to arrive at an implied relative value of $144 per share.

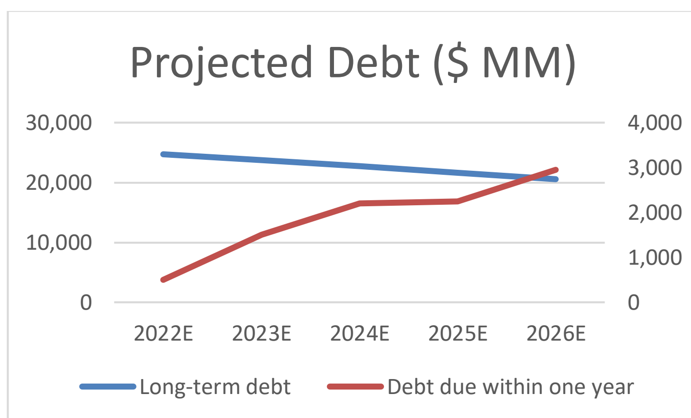
Income Statement

We expect the total revenues to increase by 34.7% in 2022E to $162 billion. The cost of revenue is forecasted to be approximately $133 billion. The EPS is expected to be $27.78, which is higher than the FactSet Consensus of $25.23. We have believe that crack spreads will continue be a higher price for longer than the other analyst. We have potentially overstated the cost of revenues, which leads to a lower net margin. We have assumed that MPC will continue to invest heavily into stock repurchases, with about $4 billion a year.

Balance Sheet

Operating assets and liabilities like accounts payable, inventories, etc., are projected to grow at the recent historical average percentage of sales. This is in large part because we do not expect any major changes to shake up the cost relative to where there are at now.

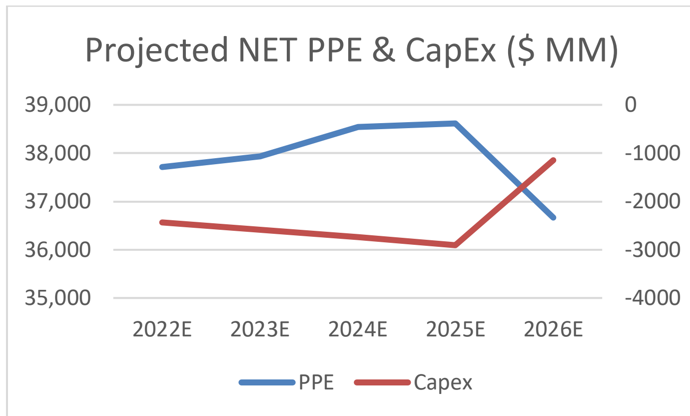
For capital expenditures, we expect heavy spending in the near-term. From there on out we have than figure rising to keep up with inflation and our potentially overstated depreciation rate until the terminal year. Depreciation was selected by averaging the historical rates and removing the lower outliers. The inflation figure used was 3.60%, which was the median Henry Fund Analyst estimate.



Source: Henry Fund Model

Despite having high cash flows over the past few years and into the near-term for the forecasted years; We believe that MPC will slowly pay off its debt, as they are

locked into relatively low-interest rates and its capital would be better spent returning capital to shareholders or making acquisitions. We do expect MPC to acquire assets to increase capacity in the near-term.



Source: Henry Fund Model

Value Drivers

We calculated the NOPLAT as a needed input to get the free cash flows and ROIC. We got the operating working capital added to the present value of operating leases, intangible assets, and net property plant and equipment to get the invested capital. We then calculated each year's free cash flow by taking that year's NOPLAT less the change in invested capital. We calculated ROIC by taking each year's NOPLAT divided by the beginning invested capital. The economic profit was also calculated on this worksheet by taking each year's beginning invested capital time ROIC less WACC.

WACC

The weighted average cost of capital was calculated using the 10-year Treasury bond as the risk-free rate. The beta used was an average of 2, 3, 3, 4, and 5-year weekly raw betas web scraped off of Bloomberg. The equity risk premium of 5.15% was Henry Fund Analysts' estimate. Using the CAPM, the cost of equity of 6.31% was solved. Marathon's pre-tax cost of debt is the yield on the firm's 10-year corporate bond. Using the marginal tax rate of 24%, the after-tax cost of debt is 1.82%. Marathon has $364,161 million in market equity value and $52,569 million in market value of debt. The market value of equity is 87.39% of market value of the firm and the market value of debt is 12.61%. After using the WACC formula, we received an estimated WACC of 5.95%.

Discounted Cash Flows Model

The discounted cash flows model used the free cash flows from the drivers' page. This model aims to discount future cash flows to the present. After we get the present value of operating assets, which was garnered from discounting the free cash flows from 2022 to perpetuity by the WACC, we subtracted the non-operating adjustments to get a value of equity. The value of equity was then divided by the number of shares outstanding to get the intrinsic value at the end of the last fiscal year. We then fractional discounting to get the intrinsic value of the share price today, which was 133. This implies a 11.23% return.

Economic Profit Model

The economic profit model used the terminal value growth of NOPLAT assumption of 3% and terminal year ROIC of 10.57%. The terminal year ROIC was calculated on the drivers' page using last year's NOPLAT divided by the beginning invested capital. We discounted the economic profit from 2022 to perpetuity by the WACC, we subtracted the non-operating adjustments to get a value of equity. The value of equity was then divided by the number of shares outstanding to get the intrinsic value at the end of the last fiscal year. We then fractional discounting to get the intrinsic value of the share price today, which was which was 133. This implies a 11.23% return.

Relative Valuation Model

The relative valuation uses peers' financial ratios that have similarities to the target company to arrive at an implied relative value. We selected Occidental Petroleum Corporation, HF Sinclair Corporation, Philips 66 Company, Valero Energy Corporation, Delek US Holdings, Inc., and Par Pacific Holdings, Inc. as peers for the Food & Staples Retailers Industry. The financial metrics used were 2023E P/S, and 2024E P/S. After getting the peers' average for each metric it is used as a multiple to arrive at the implied relative value. We multiplied the Marathon's financials

metrics times the peers' multiples and averaged these out to arrive at an implied relative value of $144 per share. This implies a return of 20.78%.

Dividend Discount Model

The dividend discount model uses the assumption that the earning per share growth will be 1.5%, to sustain growth with the economy. The terminal year ROE was solved for on the ratios' worksheet. The cost of equity was solved for on the WACC's worksheet. The future EPS and DPS were projected out on the IS worksheet. The dividends per share were discounted for 2022 to perpetuity by the cost of equity to get the intrinsic value at the end of last fiscal year. We then utilized fractional discounting to get the intrinsic value of the share price today, which was $175. This implies a return of 46.17%.

We believe MPC has potential to become a great dividends stock. We believe MPC can continue its heavy share repurchases and to raise dividends in accordance with guidance (we used guidance for dividend per share). The terminal year generated a high ROE of 31%, which could have potentially overstated the DDM calculation. We do believe the opportunity is there for MPC to use its capital to generate a great return for shareholders.

Sensitivity Analysis

We built six sensitivity tables that would help us understand the marginal change by slight differences in the models' assumptions the twelve variables were pre-tax cost of debt, risk-free rate, beta, terminal growth of pre-tax cost of debt, risk-free rate, beta, marginal tax rate, equity risk premium, terminal growth of NOPLAT, terminal ROE, terminal growth of EPS, 2023E refined gasoline growth, 2023E Midstream growth, depreciation rate, and 2026E crack spread per barrel.

The most sensitive table was the 2026E crack spread per barrel versus the depreciation rate. It is the terminal year and is the main driver in revenue. If the crack spread per barrel is even to $14.96, the stock price is down over 50%. We can also view this conversely, if the crack spread per barrel is up to $17.96, the stock price is up over 50%. We can suggest that is because of the levered situation of over $30 billion in debt and the high capital intensity of this business model.

Another interesting sensitive table is the 2023E Midstream growth, which is assuming a negative growth rate of -35%. We chose this number because it conservatively brought the segments revenue back to historical numbers, which had been relatively stable over the past 10 years. We believe it that the Russia-Ukraine situation will end in the near-term driving the Midstream's demand down. With just a 2% growth in 2023E, we would see an over 15% rise in the price.

Sanity Check

The For a sanity check we chose three liquidity ratios, asset-management leverage ratios, profitability ratios, and payout ratios. The most eye-catching ratio from the "sanity" test is the total payout ratio. We have the total payout ratio in 2022E over 100% due to over $17 billion in repurchases. The ratio is still extremely high at over 50% for every year but will continue to drop as more shares are repurchased.

RECOMMENDATION

We are recommending a **BUY** rating on Marathon Petroleum Corporation (MPC). MPC shares are trading at 119.50 per share. This allows for a sizable gain due to our recommended range of $135.00 to $140.00. We understand the many uncertainties regarding this firm's idiosyncratic and commodity volatility risks. We believe due to our bearish outlook on oil relative to street consensus and strong labor market will result in strong results for MPC in the near and long-term.

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