



Independent Stock Idea

February 3, 2010

rating: contrarian buy
s&p 500: 1103

Marathon Oil (MRO) Ready for Recovery in Demand for Diesel Fuel

<i>Symbol</i>	MRO	<i>Ebitda Next Twelve Months ending 12/31/10 (US\$mm)</i>	6,500
<i>Rating</i>	Contrarian Buy	<i>North American Natural Gas/Ebitda (%)</i>	7
<i>Price (US\$/sh)</i>	30.90	<i>Natural Gas and Oil Production/Ebitda (%)</i>	74
<i>Pricing Date</i>	2/2/10	<i>Adjusted Reserves/Production NTM</i>	10.9
<i>Shares (mm)</i>	711	<i>EV/Ebitda</i>	5.1
<i>Market Capitalization (US\$mm)</i>	22,000	<i>PV/Ebitda</i>	7.5
<i>Debt (US\$mm)</i>	11,400	<i>Undeveloped Reserves (%)</i>	36
<i>Enterprise Value (EV) (US\$mm)</i>	33,400	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	29.70
<i>Present Value (PV) (US\$mm)</i>	49,100	<i>Present Value Proven Reserves(US\$/boe)</i>	16.80
<i>Net Present Value (US\$/share)</i>	53	<i>Present Value Proven Reserves(US\$/mcf)</i>	2.80
<i>Debt/Present Value</i>	0.23	<i>Earnings Next Twelve Months (US\$/sh)</i>	2.84
<i>McDep Ratio - EV/PV</i>	0.68	<i>Price/Earnings Next Twelve Months</i>	11
<i>Dividend Yield (%/year)</i>	3.1	<i>Indicated Annual Dividend (US\$/sh)</i>	0.96
Note: Estimated cash flow and earnings tied to one-year futures prices for oil and natural gas.			
Reported results may vary widely from estimates. Estimated present value per share revised only infrequently.			
Estimated present value presumes a long-term price for oil of US\$75 a barrel and natural gas, \$8 a million btu.			
For historical research on Marathon since 2001 see http://www.mcdep.com/3mro.htm			

Summary and Recommendation

Contrarian Buy-recommended **Marathon Oil (MRO)** offers unlevered appreciation potential of 47% to a McDep Ratio of 1.0 where stock price would equal Net Present Value (NPV) of US\$53 a share. Fourth quarter results released on February 2 disclose unlevered cash flow (Ebitda) below our expectations of three months ago. Upstream costs resulted in a low Ebitda margin and downstream reflected a more depressed refining margin (see table [Next Twelve Months Operating and Financial Estimates](#)). Executive Vice President Gary Heminger explains on the earnings call that refining profits are likely to recover with rebounding demand for diesel fuel in a growing global economy. At the same time, increased reported reserves in Canadian oil sands supports NPV in an industry context judged by cash flow and reserve life (see table [Functional Cash Flow and Present Value](#)). Meanwhile, the trend for oil, 63% of the value in Marathon, continues up with futures prices for the next six years at \$86 a barrel compared to the 40-week average of \$82 (see chart [Six-Year Commodity Price Meter](#)). Seeing Marathon stock below its 200-day average of \$33 a share, we reclassify our previous Buy rating to Contrarian Buy.

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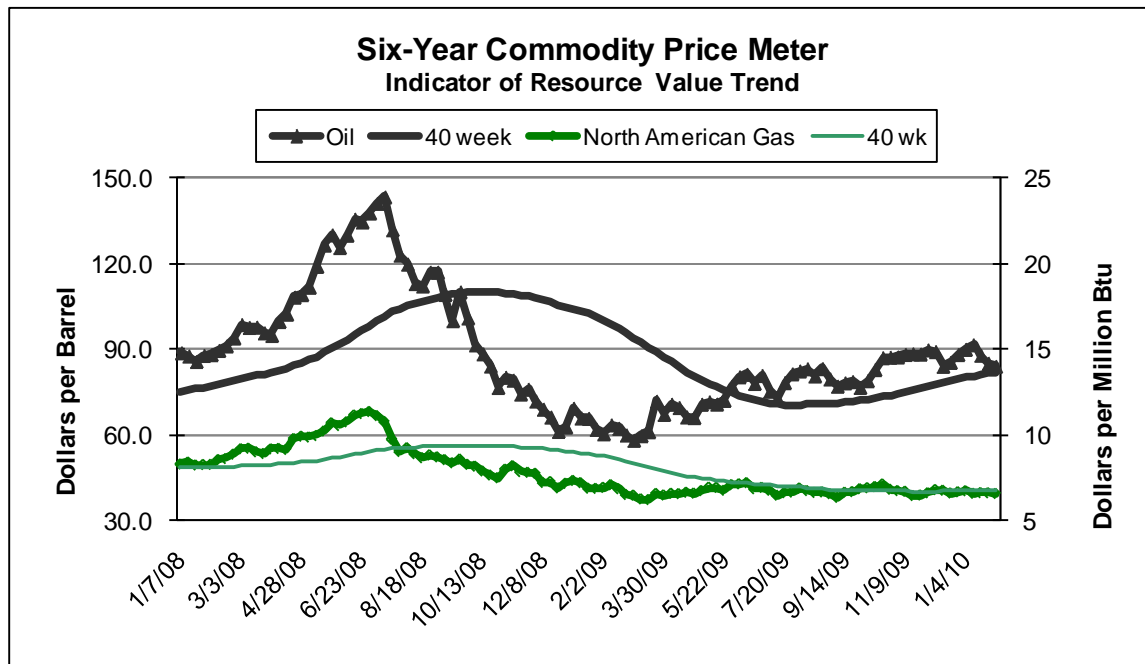
Marathon Oil Corporation									
Next Twelve Months Operating and Financial Estimates									
	Q4	Q3	Q4	Year	Q1E	Q2E	Q3E	Q4E	Next
	12/31/08	9/30/09	12/31/09	2009	3/31/10	6/30/10	9/30/10	12/31/10	Twelve
									Months
									12/31/10
Volume									
Natural Gas (mmcf)									
U.S. (or North America)	454	339	364	373	364	364	364	364	364
Overseas (or Int'l)	552	528	565	585	565	540	540	540	546
Total	1,006	867	929	958	929	904	904	904	910
Days	92	92	92	365	90	91	92	92	365
Oil (mbd)	281	265	293	280	293	293	293	293	293
Total gas & oil (bcf)	248	226	247	964	242	242	245	245	974
Total gas & oil (mbd))	449	410	448	440	448	444	444	444	445
Price									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	6.95	3.39	4.16	3.99	5.53	5.45	5.64	6.12	5.69
U.S. (or North America)	5.00	3.63	4.76	4.14	6.32	6.23	6.45	7.00	6.50
Overseas (or Int'l)	3.14	1.29	1.28	1.57	1.57	1.57	1.57	1.57	1.57
Total	3.98	2.20	2.64	2.57	3.43	3.45	3.54	3.76	3.54
Oil (\$/bbl)									
WTI Cushing	58.45	68.22	76.09	61.70	75.89	75.77	77.37	78.64	76.92
Worldwide	57.89	64.00	70.11	57.87	69.93	69.82	71.30	72.47	70.89
Total gas & oil (\$/mcf)	7.53	7.68	8.56	7.08	8.81	8.86	9.05	9.25	8.99
NY Harbor 3-2-1 (\$/bbl)	5.10	9.45	5.22	8.34	6.92	9.63	8.41	4.65	7.40
Revenue (\$mm)									
Natural Gas									
U.S. (or North America)	209	113	159	564	207	206	216	234	864
Overseas (or Int'l)	159	63	67	336	80	77	78	78	314
Total	368	176	226	900	287	284	294	312	1,178
Oil	1,497	1,560	1,890	5,920	1,844	1,861	1,922	1,953	7,581
Other	12,933	12,741	13,950	47,437	13,950	13,950	13,950	13,950	55,801
Total	14,798	14,477	16,066	54,258	16,081	16,096	16,166	16,216	64,559
Expense	12,502	13,025	14,855	49,147	14,496	14,495	14,418	14,623	58,032
Ebitda (\$mm)									
Exploration and Production	1,477	1,091	1,005	3,709	1,172	1,180	1,219	1,246	4,817
Other	819	361	206	1,402	413	421	529	347	1,710
Total Ebitda	2,296	1,452	1,211	5,111	1,585	1,601	1,748	1,593	6,527
Exploration	122	55	126	307	126	126	126	100	478
Deprec., Deplet., & Amort.	626	630	635	2,631	635	635	635	635	2,540
Other non cash									
Ebit	1,548	767	450	2,173	824	840	987	858	3,509
Interest	100	100	100	400	100	100	100	100	400
Ebt	1,448	667	350	1,773	724	740	887	758	3,109
Income Tax	430	234	123	620	254	259	310	265	1,088
Net Income (\$mm)									
Exploration and Production	364	516	480						
Other	361	171	19						
Unallocated	293	(253)	(271)						
Total	1,018	434	228	1,152	471	481	576	493	2,021
Shares (millions)	707	711	711	711	711	711	711	711	711
Per share (\$)	1.44	0.61	0.32	1.62	0.66	0.68	0.81	0.69	2.84
Ebitda Margin (E&P)	79%	63%	47%	54%	55%	55%	55%	55%	55%
Tax Rate	30%	35%	35%	35%	35%	35%	35%	35%	35%



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Marathon Oil Corporation					
Functional Cash Flow and Present Value					
	<i>NTM</i>	<i>Adjusted</i>	<i>PV/</i>	<i>Present</i>	
	<i>Ebitda</i>	<i>R/P</i>	<i>Ebitda</i>	<i>Value</i>	
North American Natural Gas	480	7.2	7.9	3,800	8%
Rest of World Natural Gas	170	12.9	9.4	1,600	3%
Oil	4,170	11.1	7.4	30,700	63%
Downstream	1,710		7.6	13,000	26%
	6,530	10.9	7.5	49,100	100%
Debt					11,400
Net Present Value (\$mm)					37,700
Shares					711
Net Present Value - Standard Estimate (US\$/sh)					53
NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh)					59





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