

**Marathon Oil Corporation**  
**Continue Buy on Valuation and Potential for Positive Surprise**

Symbol	Price	Shares	Market Cap (\$mm)	Net		McDep Ratio	EV/	EV/	P/E	Div'd	PV/
	(\$/sh)			Present Value (\$/sh)	Debt/ Present Value		Sales NTM	Ebitda NTM		NTM (%)	Ebitda NTM
MRO	21.52	310	6,670	40.00	0.37	0.71	0.4	4.7	8	4.3	6.6

McDep Ratio = Market cap and Debt to present value of oil and gas and other businesses

EV = Enterprise Value = Market Cap and Debt: \$mm 13,900

Ebitda = Earnings before interest, tax, depreciation and amortization: \$mm 2,980

NTM = Next Twelve Months Ended March 32, 2003; P/E = Stock Price to Earnings

PV = Present Value of energy businesses: \$mm 19,600

Present Value of Equity: \$mm 12,400

**Summary and Recommendation**

We continue our recommended purchase of the common shares of Marathon Oil Corporation (MRO) on the basis of low McDep Ratio, attractive dividend and the likelihood, in our opinion, that oil and gas profits will be higher than expected in 2003 and beyond. Marathon's stock price has declined while oil and gas production profits have been rising since the fourth quarter of 2001. Because the rise in retail fuel price currently seems to be lagging crude oil price, refining/marketing profits are recovering more slowly from a bottom in the first quarter of last year. As a result, investing in Marathon is a chance to participate in an energy producer stock that has not advanced in price yet. Investors may also be holding back in the expectation that there will be some decline in oil price after a possible regime change in Iraq. The surprise may be that it may come from a higher level and the drop may be less than expected because underlying world oil supply is tighter than in 20 years. Another surprise could be that as the smallest major oil, Marathon is a ready target for acquisition by a giant.

**Futures Prices Point to Rising Profits**

Our Next Twelve Months (NTM) model translates futures for natural gas, crude oil and refining crack to cash flow and earnings for Marathon (see table). Thus we substitute the market for the most variable input. As a result NTM expectations are volatile as in real life.

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**McDep Associates**  
**Independent Stock Idea**  
November 20, 2002

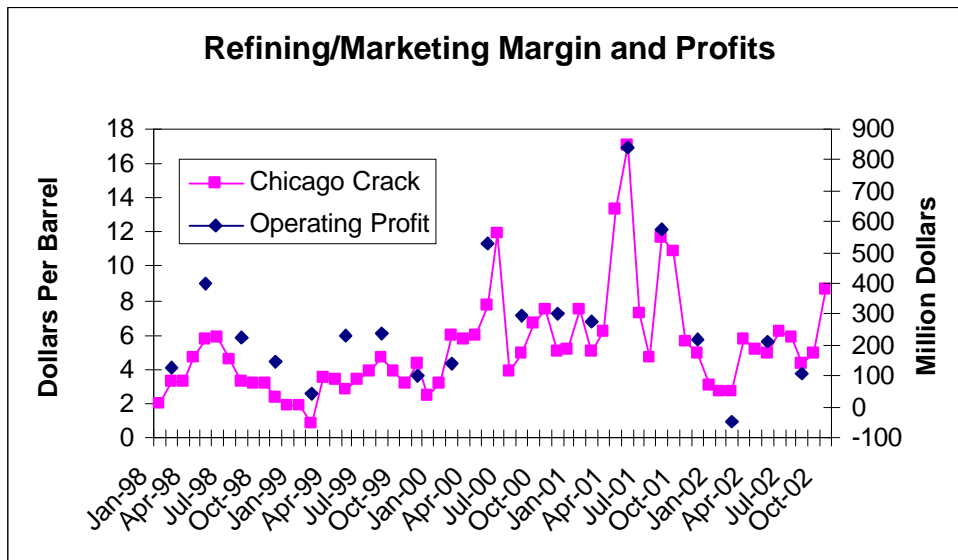
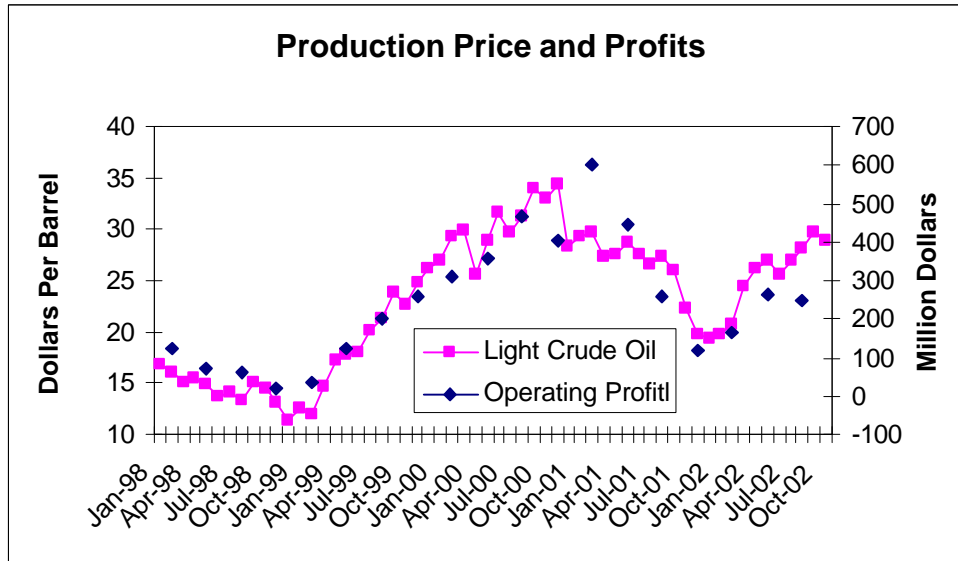
**Marathon Oil Corporation**  
**Next Twelve Months Operating and Financial Estimates**

	<i>Year</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Q2E</i>	<i>Next Twelve Months</i>
	<i>2001</i>	<i>3/31/02</i>	<i>6/30/02</i>	<i>9/30/02</i>	<i>12/31/02</i>	<i>2002E</i>	<i>3/31/03</i>	<i>6/30/03</i>	<i>12/31/03</i>
<b>Volume</b>									
Natural Gas (mmcf)									
U.S. (or North America)	<b>793</b>	787	734	710	710	<b>735</b>	710	710	<b>710</b>
Overseas (or Int'l)	<b>480</b>	522	474	458	458	<b>478</b>	458	458	<b>458</b>
Total	<b>1,273</b>	1,309	1,208	1,168	1,168	<b>1,213</b>	1,168	1,168	<b>1,168</b>
Oil (mmb)									
Oil (mbd)	<b>76</b>	19	20	17	17	<b>74</b>	17	17	<b>69</b>
Total gas & oil (bcf)	<b>209</b>	206	223	189	189	<b>202</b>	189	189	<b>189</b>
Total gas & oil (mbd)	<b>421</b>	424	424	384	384	<b>404</b>	384	384	<b>384</b>
<b>Price</b>									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	<b>3.96</b>	2.53	3.38	3.21	4.30	<b>3.36</b>	4.69	4.46	<b>4.54</b>
U.S. (or North America)	<b>3.46</b>	2.35	2.99	2.75	3.69	<b>2.93</b>	4.02	3.82	<b>3.89</b>
Overseas (or Int'l)	<b>2.97</b>	2.46	2.31	2.37	2.36	<b>2.38</b>	2.59	2.39	<b>2.31</b>
Total	<b>3.27</b>	2.39	2.72	2.60	3.17	<b>2.71</b>	3.46	3.26	<b>3.27</b>
Oil (\$/bbl)									
WTI Cushing	<b>25.95</b>	21.60	26.27	28.33	28.18	<b>26.10</b>	31.01	28.51	<b>27.67</b>
Worldwide	<b>21.15</b>	18.94	22.96	24.79	24.66	<b>22.78</b>	27.13	24.95	<b>24.19</b>
Total gas & oil (\$/mcf)	<b>35.89</b>	2.76	3.30	3.35	3.63	<b>38.46</b>	3.98	3.70	<b>42.38</b>
NY Harbor 3-2-1 (\$/bbl)	<b>6.23</b>	3.63	4.71	4.13	5.54	<b>4.50</b>	5.18	6.71	<b>5.87</b>
Chicago 3-2-1 (\$/bbl)	<b>8.07</b>	3.70	5.42	5.02					
<b>Revenue (\$mm)</b>									
Natural Gas									
U.S. (or North America)	<b>1,002</b>	166	200	180	241	<b>787</b>	257	247	<b>1,009</b>
Overseas (or Int'l)	<b>520</b>	116	100	100	99	<b>414</b>	107	99	<b>387</b>
Total	<b>1,522</b>	282	299	279	340	<b>1,201</b>	364	346	<b>1,395</b>
Oil	<b>1,612</b>	351	466	431	429	<b>1,677</b>	461	429	<b>1,669</b>
Other	<b>29,959</b>	5,821	7,362	7,808	10,145	<b>31,135</b>	8,339	7,997	<b>32,544</b>
Total	<b>33,093</b>	6,454	8,127	8,518	10,914	<b>34,013</b>	9,164	8,773	<b>35,608</b>
<b>Expense</b>									
Fixed	<b>469</b>	132	153	143	143	<b>570</b>	143	143	<b>571</b>
Variable	<b>469</b>	132	153	143	154	<b>582</b>	166	156	<b>616</b>
Other	<b>28,326</b>	5,732	7,098	7,608	9,877	<b>30,314</b>	8,088	7,673	<b>31,443</b>
<b>Ebitda (\$mm)</b>									
Exploration and Production	<b>2,197</b>	369	460	425	472	<b>1,726</b>	517	477	<b>1,878</b>
Other	<b>1,633</b>	89	264	200	268	<b>821</b>	250	325	<b>1,101</b>
Total Ebitda	<b>3,830</b>	458	724	625	740	<b>2,546</b>	767	801	<b>2,978</b>
Exploration	<b>144</b>	57	44	29	50	<b>180</b>	40	40	<b>160</b>
Deprec., Deplet., & Amort.	<b>1,235</b>	294	308	292	292	<b>1,186</b>	292	292	<b>1,168</b>
<b>Ebit</b>	<b>2,451</b>	107	372	304	398	<b>1,180</b>	435	469	<b>1,650</b>
Interest	<b>187</b>	64	76	75	75	<b>290</b>	75	75	<b>300</b>
<b>Ebt</b>	<b>2,264</b>	43	296	229	323	<b>890</b>	360	394	<b>1,350</b>
Income Tax	<b>794</b>	15	104	80	113	<b>312</b>	126	138	<b>473</b>
<b>Net Income (\$mm)</b>									
Exploration and Production	<b>1,435</b>	165	262	250					
Other	<b>1,248</b>	(26)	231	137					
Unallocated	<b>(1,213)</b>	(111)	(301)	(238)					
Total	<b>1,470</b>	28	192	149	210	<b>579</b>	234	256	<b>878</b>
<b>Shares (millions)</b>	<b>309</b>	310	310	310	310	<b>310</b>	310	310	<b>310</b>
Per share (\$)	<b>4.75</b>	0.09	0.62	0.48	0.68	<b>1.87</b>	0.75	0.83	<b>2.83</b>

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**Historical Results Demonstrate Volatility**

The relationship is demonstrated in hindsight. Crude oil price and refining crack (product price minus crude oil) explain most of the variation in past quarterly results (see Charts).



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### Value Estimate Less Volatile

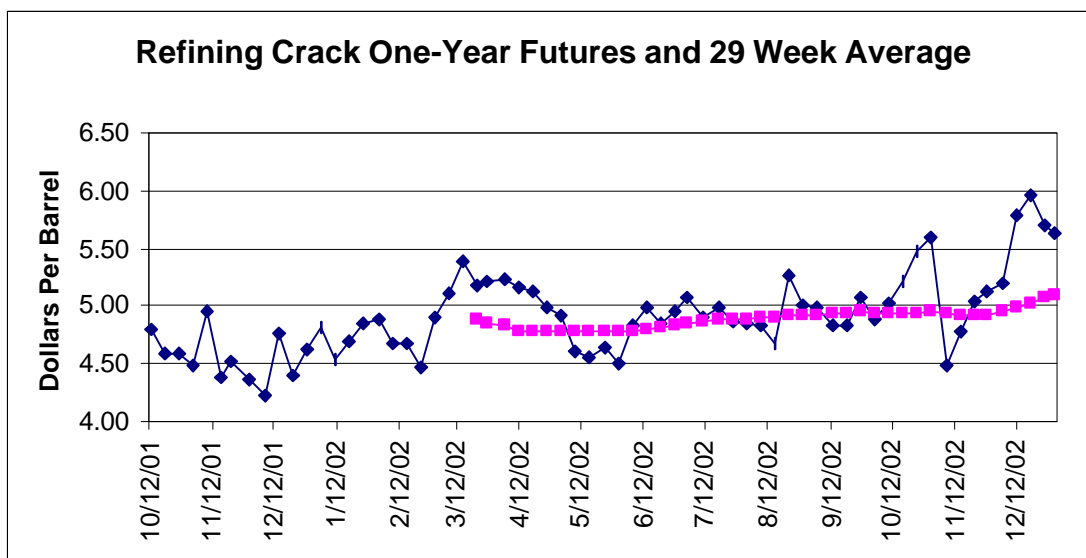
Long-term value depends on more than NTM projections. Experimenting with weekly calculations of present value for natural gas royalty trusts we have observed that six-year futures influence the value estimate in similar fashion. The important distinction is that six-year futures are less volatile.

We don't actually apply six-year futures directly to valuing Marathon, but rather assess a present value to cash flow multiple that takes account of many factors including the relationship of NTM futures to six-year futures. In reality the cash flow multiple is also volatile, but present value is less so. For example our estimate of \$40 per share today compares to \$42 a year ago when Marathon's stock price was \$30.

The trend in six-year futures appears to be up for both natural gas and oil as we have detailed elsewhere (see *Meter Reader*, January 2, 2003). Thus, already strong resource values may be getting stronger.

There are no six-year futures that can be combined to measure refining crack. Instead we make do with NTM futures. Current expectations are modest, but in a rising trend (see Chart). Between the refinery rack and the automobile, home or factory, there may be more lags in response to crude oil price changes.

Kurt H. Wulff, CFA



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