

Rating: Hold  
 S&P 500: 1513

## **Marathon Oil Corporation**

### **Downgrade to Hold from Buy on Price**

<i>Symbol</i>	MRO	<i>Ebitda Next Twelve Months ending 3/31/08 (US\$m)</i>	7,800
<i>Rating</i>	Hold	<i>North American Natural Gas/Ebitda (%)</i>	11
<i>Price (US\$/sh)</i>	113.45	<i>Natural Gas and Oil Production/Ebitda (%)</i>	53
<i>Pricing Date</i>	5/17/07	<i>Adjusted Reserves/Production NTM</i>	8.1
<i>Shares (mm)</i>	347	<i>EV/Ebitda</i>	5.8
<i>Market Capitalization (US\$m)</i>	39,400	<i>PV/Ebitda</i>	5.7
<i>Debt (US\$m)</i>	6,200	<i>Undeveloped Reserves (%)</i>	32
<i>Enterprise Value (EV) (US\$m)</i>	45,600	<i>Natural Gas and Oil Ebitda (US\$/boe)</i>	32.00
<i>Present Value (PV) (US\$m)</i>	44,400	<i>Present Value Proven Reserves(US\$/boe)</i>	18.90
<i>Net Present Value (US\$/share)</i>	110	<i>Present Value Proven Reserves(US\$/mcf)</i>	3.15
<i>Debt/Present Value</i>	0.14	<i>Earnings Next Twelve Months (US\$/sh)</i>	11.06
<i>McDep Ratio - EV/PV</i>	1.03	<i>Price/Earnings Next Twelve Months</i>	10
<i>Dividend Yield (%/year)</i>	1.7	<i>Indicated Annual Dividend (US\$/sh)</i>	1.92

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\$60 a barrel and natural gas, \$10 a million btu.

For historical research on Marathon since 2001 see <http://www.mcdep.com/3mro.htm>

### **Summary and Recommendation**

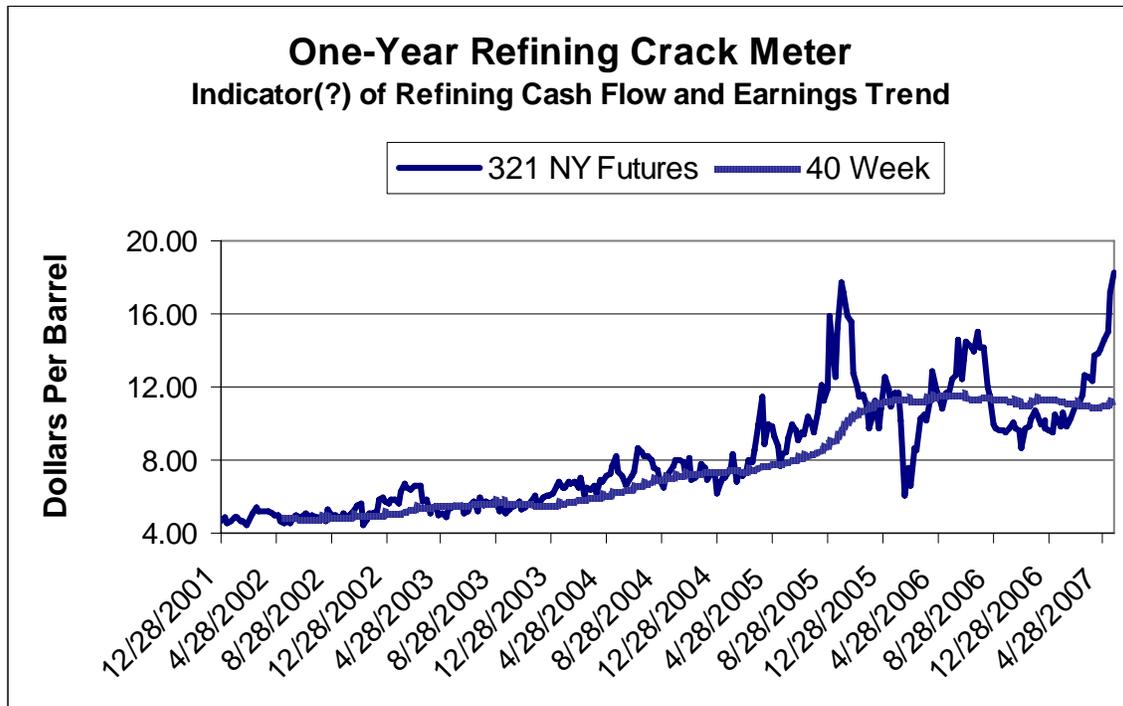
Because **Marathon Oil (MRO)** stock price exceeds net present value (NPV) of \$110 a share, we change our rating to Hold from Buy. At NPV a stock would theoretically earn an unlevered return of 7% a year above inflation and “the attributes of the underlying business are reflected in the current price of the stock” as we say in our disclosures. We may raise our estimates of present value that have not changed for the industry in a year. We also remain bullish long-term with our vision of \$150 oil in 2010. At the same time, among our buy recommendations, Marathon had the highest proportion of value, 43%, in the downstream refining/marketing business where profit margins are the most volatile (see table Functional Cash Flow and Present Value). The one-year refining crack has “gone parabolic”, a pattern that may lead to further increases, but is also likely to settle back steeply eventually (see chart One-Year Refining Crack Meter). On today’s indications, earnings for the current quarter could be more than \$5 a share rather than near \$3 in the assumptions we have been using (see table Next Twelve Months Operating and Financial Estimates). Though our downgrade of Marathon stock may be premature we continue with buy recommendations of other companies with related, though less concentrated, exposure to a powerful gasoline price trend.

Kurt H. Wulff, CFA

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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	880	5.2	5.2	4,600	10%
Rest of World Natural Gas	320	15.7	8.1	2,600	6%
Oil	2,970	7.5	6.1	18,200	41%
Downstream	3,660		5.2	19,000	43%
	7,830	8.1	5.7	44,400	100%
Debt					6,200
Net Present Value (\$mm)					38,200
Shares					347
Net Present Value - Standard Estimate (US\$/sh)					110
Net Present Value - Approximation by Correlation (US\$/sh)					113



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

	<i>Q2</i>	<i>Year</i>	<i>Q1</i>	<i>Q2E</i>	<i>Q3E</i>	<i>Q4E</i>	<i>Year</i>	<i>Q1E</i>	<i>Next Twelve Months</i>
	<i>6/30/06</i>	<i>2006</i>	<i>3/31/07</i>	<i>6/30/07</i>	<i>9/30/07</i>	<i>12/31/07</i>	<i>2007E</i>	<i>3/31/08</i>	<i>3/31/08</i>
<b>Volume</b>									
Natural Gas (mmcf)									
U.S. (or North America)	523	<b>532</b>	512	512	512	512	<b>512</b>	512	<b>512</b>
Overseas (or Int'l)	277	<b>315</b>	337	277	197	352	<b>291</b>	337	<b>291</b>
Total	800	<b>847</b>	849	789	709	864	<b>803</b>	849	<b>803</b>
Oil (mbd)	258	<b>231</b>	198	198	198	250	<b>211</b>	250	<b>224</b>
Total gas & oil (bcf)	214	<b>814</b>	183	180	175	217	<b>755</b>	211	<b>783</b>
Total gas & oil (mbd)	391	<b>372</b>	340	330	316	394	<b>345</b>	392	<b>358</b>
<b>Price</b>									
Natural gas (\$/mcf)									
Henry Hub (\$/mmbtu)	6.81	<b>7.23</b>	6.81	7.68	8.19	9.02	<b>7.92</b>	9.90	<b>8.70</b>
U.S. (or North America)	5.35	<b>5.76</b>	5.91	6.66	7.11	7.83	<b>6.88</b>	8.59	<b>7.54</b>
Overseas (or Int'l)	5.19	<b>5.27</b>	4.91	5.19	4.10	4.90	<b>4.84</b>	4.91	<b>4.84</b>
Total	5.29	<b>5.58</b>	5.51	6.15	6.27	6.63	<b>6.14</b>	7.13	<b>6.56</b>
Oil (\$/bbl)									
WTI Cushing	70.47	<b>66.05</b>	58.08	63.01	64.93	67.04	<b>63.26</b>	68.33	<b>65.83</b>
Worldwide	63.95	<b>57.96</b>	51.07	55.41	57.09	58.95	<b>55.86</b>	60.09	<b>58.07</b>
Total gas & oil (\$/mcf)	8.83	<b>8.11</b>	7.26	8.00	8.30	8.66	<b>8.08</b>	8.97	<b>8.51</b>
NY Harbor 3-2-1 (\$/bbl)	15.39	<b>10.50</b>	11.68	27.09	23.12	13.76	<b>18.91</b>	13.07	<b>19.26</b>
<b>Revenue (\$mm)</b>									
Natural Gas									
U.S. (or North America)	255	<b>1,118</b>	272	310	335	369	<b>1,286</b>	396	<b>1,410</b>
Overseas (or Int'l)	131	<b>605</b>	149	131	74	159	<b>513</b>	149	<b>513</b>
Total	385	<b>1,723</b>	421	441	409	527	<b>1,799</b>	545	<b>1,922</b>
Oil	1,501	<b>4,882</b>	910	998	1,040	1,356	<b>4,304</b>	1,352	<b>4,746</b>
Other	16,403	<b>58,943</b>	11,671	11,671	11,671	11,671	<b>46,683</b>	11,671	<b>46,683</b>
Total	18,290	<b>65,548</b>	13,002	13,110	13,120	13,554	<b>52,786</b>	13,567	<b>53,351</b>
<b>Expense (\$mm)</b>									
Ebitda (\$mm)									
Exploration and Production	1,305	<b>4,338</b>	904	950	956	1,130	<b>3,941</b>	1,138	<b>4,175</b>
Other	1,460	<b>4,367</b>	639	1,168	1,128	727	<b>3,662</b>	639	<b>3,662</b>
Total Ebitda	2,765	<b>8,705</b>	1,543	2,118	2,084	1,857	<b>7,603</b>	1,777	<b>7,836</b>
Exploration	66	<b>365</b>	61	90	90	90	<b>331</b>	90	<b>360</b>
Deprec., Deplet., & Amort.	369	<b>1,533</b>	393	393	393	393	<b>1,572</b>	393	<b>1,572</b>
Other non cash		<b>(350)</b>							
<b>Ebit</b>	2,330	<b>7,157</b>	1,089	1,635	1,601	1,374	<b>5,700</b>	1,294	<b>5,904</b>
Interest		<b>24</b>							
<b>Ebt</b>	2,330	<b>7,133</b>	1,089	1,635	1,601	1,374	<b>5,700</b>	1,294	<b>5,904</b>
Income Tax	815	<b>2,496</b>	381	572	560	481	<b>1,995</b>	453	<b>2,067</b>
<b>Net Income (\$mm)</b>									
Exploration and Production	659	<b>2,015</b>	385						
Other	934	<b>2,811</b>	364						
Unallocated	(79)	<b>(190)</b>	(41)						
Total	1,514	<b>4,636</b>	708	1,063	1,041	893	<b>3,705</b>	841	<b>3,838</b>
<b>Shares (millions)</b>	364	<b>361</b>	347	347	347	347	<b>347</b>	347	<b>347</b>
Per share (\$)	4.16	<b>12.85</b>	2.04	3.06	3.00	2.57	<b>10.68</b>	2.42	<b>11.06</b>
Ebitda Margin (E&P)	69%	<b>66%</b>	68%	66%	66%	60%	<b>65%</b>	60%	<b>63%</b>
Tax Rate	35%	<b>35%</b>	35%	35%	35%	35%	<b>35%</b>	35%	<b>35%</b>

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