



Occidental Petroleum Corp.

Analyst: Jack Flaherty

Minutemen Fixed Income Fund

Investment Thesis

We recommend an overweight position on Occidental Petroleum's (OXY) 2.9% 2024 senior unsecured notes. OXY is an independent E&P company engaged in crude oil and natural gas production as well as basic chemicals and vinyls. OXY holds around 3.8 billion BOE reserves, primarily crude oil in the U.S. It is the largest player in the Permian basin boasting a daily production of ~500 MBOE/day as of Q1 20. A poorly timed and expensive acquisition of Anadarko has added considerable doubt in OXY's management and a heavy debt profile. We believe this has left OXY's short term debt undervalued. The current pricing environment is not ideal for E&P companies, however we believe that OXY's diversity of revenue and hedging strategies puts them above their peers. OXY also will have the liquidity needed to get through a tough maturity schedule in 2022. Finally, we believe there are still unrealized synergies from OXY's 2019 acquisition of Anadarko that will show as production normalizes. We expect the spread on OXY's 2.9% 24's to tighten 50-75 bps by YE22, with continued tightening as the maturity date approaches.

Figure 1: Capitalization Table

OXY Capitalization Table (mm)						
LTM Adj. EBITDA	8,544.0		Debt/EV	76%		
Outstanding Debt and Leverage Metrics						
Type	Rate	Maturity	Debt Outstanding	xEbitda	Price	Yield
Revolver	1.4%	01/31/23	-			1.40%
Senior Unsecured Notes						
2021 notes	4.1%	02/01/21	166.6		99.58	6.09%
2021 notes	3.0%	02/08/21	27.1		99.54	3.18%
2021 notes	4.9%	03/15/21	123.3		100.13	3.52%
2021 loan	1.6%	08/08/21	1.1		100.00	1.60%
2021 notes	2.6%	08/13/21	350.1		99.60	3.14%
2022 notes	3.1%	02/15/22	813.7		98.10	4.71%
2022 notes	2.6%	04/15/22	228.7		98.39	3.78%
2022 notes	2.7%	08/15/22	1,898.5		95.96	5.15%
2022 notes	2.7%	08/15/22	1,052.1		95.22	4.49%
2023 notes	8.8%	01/15/23	22.3		95.38	11.20%
2023 notes	2.7%	02/15/23	1,139.0		94.79	5.19%
2024 notes	7.0%	07/01/24	582.5		102.96	6.03%
2024 notes	3.5%	07/15/24	233.1		89.87	6.61%
2024 notes	2.9%	08/15/24	3,000.0		90.31	5.81%
2025-2049 notes			25,473.9			
Total Debt			35,112.0	4.1x		
Market Capitalization			10,988			
Less: Cash			(1,896.0)			
Enterprise Value			44,204	5.2x		

Source: Company Filings, MFIF Analysis, Bloomberg

Security Data

Bond Maturity: 8/15/2024

Rating: Ba2 / BB+

Rank: Senior Unsecured

Price: \$90.31

Yield-to-worst: 5.81%

Call Date: 7/15/2024

Coupon: 2.9 %

Z-Spread: 546 bps

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Industry Overview

The energy industry has been one of, if not the hardest hit sector due to the COVID-19 pandemic and aftermath. The unparalleled decrease in demand for both crude oil and natural gas has placed a strain on all companies in the industry, especially E&P companies, which have suffered due to record low commodity prices. Politics also play a role in the industry, both domestically and internationally. Although prices have made significant recovery since Q2 lows, a complete recovery for the industry is unlikely to occur in the near term.

Investment Rationale and Catalysts

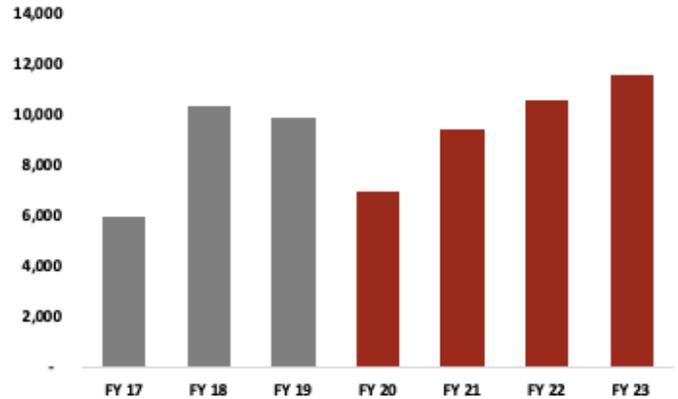
Diversity of revenue and hedges provide income stability

In January, management set up three-way costless collars on oil and two-way costless gas collars for FY20 and FY21. Current hedges for Q4 and FY21 amount to just under a third of estimated oil and half of natural gas production. When Brent prices are below \$45 (currently ~\$42), these hedges enhance cashflow by close to \$325 million per quarter. The long put and short call on the gas collars sit at \$2.50 and \$3.64 respectively (price currently ~\$2.75). With the volatility and slow recovery of energy prices, these hedges provide better downside protection than its peers for little to no additional cost (CLR has no hedges on oil, APA three-way collars at \$46/\$20/\$15, WPX has a number of hedges overall less favorable). With an expected breakeven price in the mid to high thirties for FY21, OXY is in great shape to not only be profitable but also add extra income. As far as revenue diversity, OxyChem has provided a lot of stability over the years, even this year through shutdowns, with revenue for FY20 projected to fall only about 8%. The majority of OxyChem operations are for construction related goods, an industry which is projected to bounce back in 2021-2022 after a rough 2020. Although the midstream and marketing operations do rely on commodity prices, it is less volatile than production operations. With about 40% of sales coming from these two operations, OXY has both of these to fall back on in weak pricing environments.

Divestitures and preferred stock provide liquidity to bypass 2022 debt wall

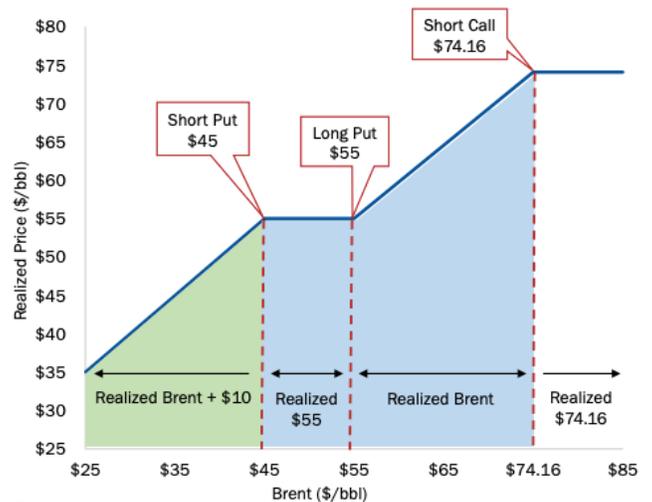
Much of the doubt around OXY has to do with its heavy debt burden. With a maturity wall of ~\$4.4 bn in 2022, OXY has a tough task ahead of them. We believe that OXY has the means to pay down this debt using divestitures as the main source of cash. OXY has done a great job of selling sub-sectors of its business that are non-essential, less profitable, and less synergistic. While this may negatively impact OXY's top line in a minor way, it will positively impact their bottom line while adding the liquidity needed to pay off debt. OXY projects \$2.7-\$3.7 bn divestitures by YE21. Management has sold ~\$7.2 bn in assets since the deal, and almost all of it has gone towards debt reduction. OXY also has the option to issue an additional \$2 bn in preferred stock as part of an acquisition financing deal with Berkshire Hathaway, and although expensive (8% dividend), this is something OXY will do if it is necessary. Finally, OXY currently has a \$5 bn IG

Figure 2: Adj. EBITDAX Projections



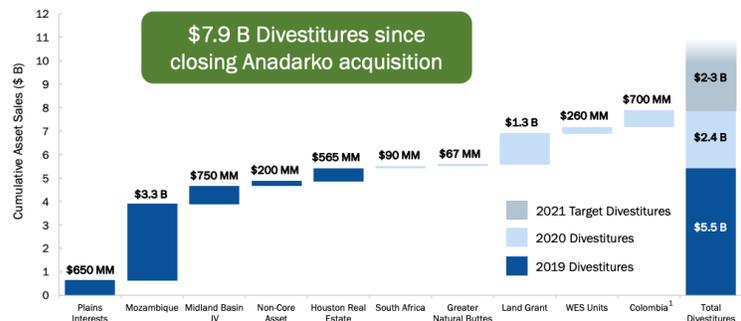
Source: Company Filings, MFIF. Analysis

Figure 3: OXY Three-way Oil Collars (\$/Bbl)



Source: Company Filings

Figure 4: Divestitures



Source: Company Filings

style credit facility with no payments outstanding. Although this matures in 2023, we believe that if necessary, OXY would be able to get a similar credit facility, especially considering the current one was issued shortly after the Anadarko deal, when OXY’s debt burden was significantly higher and consensus outlook for the company was very negative. We expect this to be realized starting in 2H 2021, as OXY chips away at the debt wall and shows ability to pass it. This will continue to be realized through FY22.

Anadarko related synergies yet to be fully realized due to current environment

Although the Anadarko deal was a poor decision by OXY, there are still a number of synergies between the companies. The deal was finalized in during Q3 2019 and as expected took some time to work out the kinks and begin the process of operating as a unit. However, OXY made major production and spending cuts in Q1 20 and have been operating at even lower levels since. This did not allow the market to see a lot of the compatibility and cost saving measures that the acquisition brought. At the time of the deal, management expected to see a 10% decrease in drilling and completed well cost, which haven’t been seen due to the low levels of drilling this year. As production increases, we also expect to see better supply chain optimization, SG&A reductions (corporate function consolidation), and up to a 5% savings in operating/capital spending. Furthermore, these estimates don’t account for the joint expertise of the two companies. We expect this to be realized by YE22, as increased production shows better than expected bottom line growth.

Relative Valuation

We believe that OXY is positioned fairly well in a competitive industry. For the reasons previously stated, OXY is in a stronger position than its valuation shows. Currently, OXY’s 24’s are trading ~150 bps wide of CLR’s 24’s and ~250 bps wide of APA’s 23’s as well as WPX’s 24’s. As a base, we expect this spread to tighten between 50 and 75 bps, however, we wouldn’t be surprised to see the spread tighten further as the maturity date approaches. OXY has the best revenue stability of these peers, with superior hedge positions as well as revenue diversity. The biggest driver of this tightening is OXY’s ability to pay down near term debt, which we believe they will have the liquidity for. We aren’t saying OXY is a better company than these peers, however the valuation provides a strong upside in the short term. WPX’s successful merger with Devon puts them in a very strong position going into 2021, however at the current price, there is little to no room for tightening. Similarly, APA and CLR are already trading close to par as the maturity date approaches. We are confident in OXY’s ability and resolve to pay down a daunting 2022 debt wall, leading to a 50-75 bps tightening in spread in by YE22, with continued tightening as the maturity date approaches.

Risks to Thesis

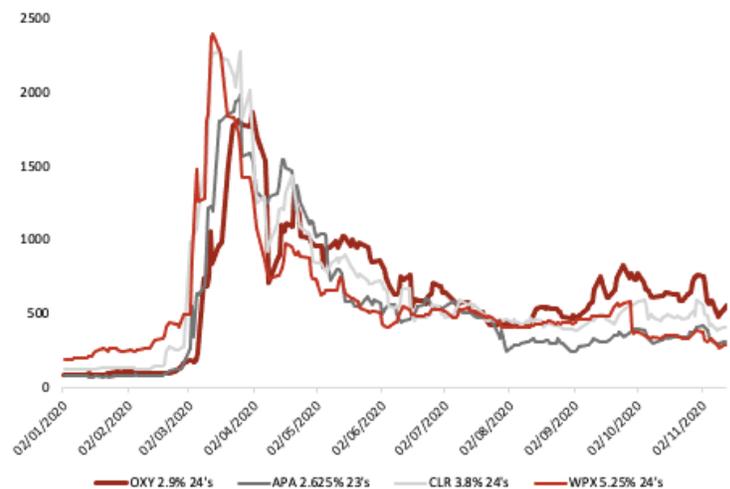
- Material downward change in supply and/or demand for crude oil and natural gas
- Unforeseen actions taken by OPEC+ and other international oil and gas producers
- Changes in legislation, political climate, or trade agreements that would act as a tailwind for OXY

Figure 5: Comparable Companies Analysis

Comp (in millions)	OXY	APA	CLR	WPX
Market Cap	10,988	3,900	5,100	3,400
Debt	35,112	9,150	5,640	3,210
Cash	1,896	162	21	195
EV	44,204	12,888	10,719	6,415
LTM Revenue	19,728	4,570	2,960	1,480
LTM Adj. EBITDA	8,544	2,260	1,940	233
Net Debt/Adj. EBITDA	3.9x	4.0x	2.9x	12.9x
LTM FCF	223	(50)	(12)	167
FCF/Debt	0.6%	-0.5%	-0.2%	5.2%
Individual Securities				
Rating	Ba2/BB+	Ba1/BB+	Ba1/BB+	B1/BB-
Coupon	2.900%	2.625%	3.800%	5.25%
Maturity	08/15/2024	01/15/2023	06/01/2024	09/15/2024
Price	90.31	98.89	98.25	106.85
YTW	5.81%	3.16%	4.34%	3.21%
Z-Spread	546 bps	289 bps	400 bps	287 bps

Source: Bloomberg, Company Filings, MFIF Analysis

Figure 6: Comparable Z-Spreads



Source: Bloomberg, MFIF Analysis

Summary Model

Occidental Petroleum Corp Summary Model (millions)	Historicals			Projections			
	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 23
Revenue	13,274	18,934	21,232	17,285	19,047	20,896	22,849
% Growth		42.6%	12.1%	-18.6%	10.2%	9.7%	9.3%
Oil and gas operating expense	(2,427)	(2,761)	(3,246)	(2,986)	(2,625)	(2,879)	(3,149)
Transportation expenses	(175)	(152)	(621)	(1,471)	(844)	(926)	(1,012)
Chemical and midstream cost of sales	(2,938)	(2,833)	(2,791)	(2,437)	(2,625)	(2,674)	(2,924)
Purchased commodities	(54)	(822)	(1,679)	(1,233)	(1,219)	(1,337)	(1,462)
SG&A	(546)	(585)	(882)	(831)	(750)	(823)	(900)
Other operating and non-operating expense	(878)	(1,028)	(1,425)	(788)	(1,031)	(1,131)	(1,237)
Depreciation, depletion, and ammortization	(4,002)	(3,977)	(5,981)	(8,259)	(7,937)	(8,292)	(8,709)
Asset impairments and other charges	(545)	(561)	(1,361)	(10,996)	-	-	-
Taxes other than on income	(311)	(439)	(707)	(556)	(525)	(576)	(630)
Anadarko acquisition-related costs	-	-	(1,647)	(302)	-	-	-
Exploration expense	(82)	(110)	(246)	(131)	(131)	(144)	(157)
EBIT	1,316	5,666	646	(12,704)	1,362	2,115	2,671
Operating Margin	9.9%	29.9%	3.0%	-73.5%	7.1%	10.1%	11.7%
Adjusted EBIT	1,861	6,227	3,654	(1,406)	1,362	2,115	2,671
Operating Margin	14.0%	32.9%	17.2%	-8.1%	7.1%	10.1%	11.7%
Interest expense	(345)	(389)	(1,066)	(1,205)	(1,521)	(1,418)	(1,321)
Other expense, net	357	331	606	(310)	320	320	320
Pre tax income	1,328	5,608	186	(14,219)	161	1,017	1,670
Provision (benefit) for income taxes	(17)	(1,477)	(693)	1,925	(39)	(244)	(401)
Loss from discontinued operations	-	-	(15)	(1,335)	-	-	-
Net income	1,311	4,131	(522)	(13,630)	122	773	1,269

EBITDAX Reconciliation							
EBIT	1,316	5,666	646	(12,704)	1,362	2,115	2,671
(+) D&A, depletion, and accretion	4,002	3,977	5,981	8,259	7,937	8,292	8,709
(+) Exploration expenses	82	110	246	131	131	144	157
(+) Acquisition cost	-	-	1,647	302	-	-	-
(+) Asset impairments	545	561	1,361	10,996	-	-	-
Adjusted EBITDAX	5,945	10,314	9,881	6,984	9,430	10,551	11,537
% Growth		73.5%	-4.2%	-29.3%	35.0%	11.9%	9.3%
Margin	44.8%	54.5%	46.5%	40.4%	49.5%	50.5%	50.5%

Balance Statement Snapshot							
Cash and cash equivalents	1,672	3,033	3,032	672	5,563	6,937	10,741
Total current assets	8,270	9,932	18,681	8,987	13,803	16,040	20,589
PP&E	31,174	31,437	80,469	66,908	61,813	58,044	54,943
Total Current Liabilities	7,400	7,412	14,949	6,827	6,502	7,074	7,577
Total Debt	9,328	10,201	38,537	35,112	34,444	30,451	29,290

FCF Reconciliation							
Cash from operating activities	4,861	7,669	7,375	4,281	7,862	8,878	9,816
(-) Capital expenditures	(3,599)	(4,975)	(6,355)	(2,391)	(2,842)	(4,523)	(5,608)
FCF	1,262	2,694	1,020	1,890	5,020	4,354	4,209

Credit Metrics							
Debt/EBIT	7.1x	1.8x	59.7x	-2.8x	25.3x	14.4x	11.0x
Debt/Adjusted EBITDAX	1.6x	1.0x	3.9x	5.0x	3.7x	2.9x	2.5x
FCF/Debt	13.5%	26.4%	2.6%	5.4%	14.6%	14.3%	14.4%

Capitalization Table

OXY Capitalization Table (mm)						
LTM Adj. EBITDA	8,544.0				Debt/EV	79%
Outstanding Debt and Leverage Metrics						
Type	Rate	Maturity	Debt Outstanding	xEbitda	Price	Yield
Revolver	1.4%	01/31/23	-			1.40%
Senior Unsecured Notes						
2021 notes	4.1%	02/01/21	166.6		99.58	6.09%
2021 notes	3.0%	02/08/21	27.1		99.54	3.18%
2021 notes	4.9%	03/15/21	123.3		100.13	3.52%
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2024 notes	3.5%	07/15/24	233.1		89.87	6.61%
2024 notes	2.9%	08/15/24	3,000.0		90.31	5.81%
2025 notes	3.5%	06/15/25	750.0		90.20	5.98%
2025 notes	8.0%	07/15/25	500.0		104.15	6.94%
2025 notes	5.9%	09/01/25	900.0		97.66	6.45%
2026 notes	5.6%	03/15/26	1,081.9		94.58	6.78%
2026 notes	3.4%	04/15/26	1,150.0		86.02	6.51%
2026 notes	3.2%	08/15/26	1,000.0		83.84	6.63%
2026 debentures	7.5%	10/15/26	88.2		94.41	8.73%
2027 debentures	3.0%	02/15/27	750.0		83.89	6.26%
2027 debentures	8.5%	07/15/27	500.0		105.28	7.48%
2027 debentures	7.1%	10/15/27	122.6		95.91	7.90%
2027 debentures	7.0%	11/15/27	29.8		81.65	10.81%
2028 debentures	6.6%	01/15/28	13.8		88.16	8.89%
2028 debentures	7.2%	04/01/28	82.0		94.44	8.22%
2028 debentures	7.2%	05/15/28	224.3		96.11	7.85%
2028 debentures	6.4%	09/01/28	600.0		97.73	6.75%
2029 debentures	8.5%	02/15/29	115.7		100.87	8.30%
2029 debentures	7.2%	03/15/29	126.0		93.87	8.23%
2029 debentures	8.0%	04/15/29	80.9		96.29	8.58%
2029 debentures	3.5%	08/15/29	1,500.0		82.27	6.15%
2030 debentures	8.9%	07/15/30	1,000.0		106.82	7.85%
2030 debentures	6.6%	09/01/30	1,500.0		97.01	7.05%
2031 debentures	7.5%	05/01/31	869.6		100.62	7.41%
2031 debentures	7.9%	09/15/31	484.7		101.23	7.70%
2036 debentures	6.5%	09/15/36	1,734.2		91.31	7.38%
2036 debentures	0.0%	10/10/36	2,270.3		45.60	5.00%
2039 notes	4.3%	01/01/39	750.0		76.96	6.43%
2039 notes	8.0%	06/01/39	325.0		100.40	7.91%
2040 notes	6.2%	06/01/40	750.0		90.67	7.09%
2044 notes	4.5%	01/01/44	625.0		78.20	6.28%
2045 notes	4.6%	06/01/45	750.0		78.43	6.37%
2046 notes	6.6%	01/01/46	1,100.0		91.82	7.31%
2046 notes	4.4%	06/01/46	1,200.0		76.72	6.24%
2047 notes	4.100%	01/01/47	750.0		72.96	6.20%
2048 notes	4.2%	06/01/48	1,000.0		75.28	6.06%
2049 notes	4.4%	01/01/49	750.0		76.46	6.16%
Total Debt			35,112.0	4.1x		
Market Capitalization			10,988			
Less: Cash			(1,896.0)			
Enterprise Value			44,204	5.2x		