

# Valero Energy Corporation (NYSE: VLO)

Sector: Energy



<b>Target Price</b>	<b>Current Price</b>	<b>52 Week High</b>	<b>52 Week Low</b>	<b>P/E</b>	<b>Market Cap.</b>	<b>Dividend Yield</b>	<b>Beta</b>
\$98	\$80.75	\$82.19	\$57.57	17.65	\$36.084B	3.34%	.99

## Business Description

Valero Energy (VLO) is an independent petroleum refining and ethanol producing company based in San Antonio, TX. VLO operates in the US, Canada, U.K., and Ireland. The company owns and operates 15 petroleum refineries and 11 ethanol plants.

Refining and ethanol contribute 95% and 5% of total revenues, respectively. The company's major products are transportation fuels, of which gasoline and diesel contribute the most to revenues. Valero is a majority-owner of Valero Energy Partners LP (VLP), a midstream master limited partnership which serves as Valero's primary vehicle to expand the transportation and logistics assets supporting its business.

## Investment Thesis

We believe Valero Energy Corporation presents a strong buying opportunity under the current macroeconomic environment. They currently possess a strong liquidity position which will provide significant protection if an industry downturn were to occur. Demand for petroleum products is expected to expand as the overall economy improves and industrial activity picks up. As the world's largest independent refinery, Valero Energy primarily relies on the spread between crude oil and the finished products in order to make money. This differential has remained relatively constant historically is expected to do so in the foreseeable future. Valero Energy fits our investment prospectus well and will continue to provide steady profit margins, dividends and quality products during our 10 year investment horizon.

## Industry Trends

During the past five years, energy companies have experienced declining profitability due to the high volatility of input costs. In the next five years to 2022, petroleum production, consumption and fuel prices are expected to increase in the USA. These factors will allow the industry to recover, as industry-wide revenues is projected to increase at an annualized rate of ~1.5%. At a global scale, demand for petroleum products will be sustained as economies are improving simultaneously.

## Valuation Assumptions

WACC: 8.00%

Terminal Growth Rate: 1.5%

Projected Revenue Growth Rate:

15% for 2017 and 2% Thereafter

## Key Financials:

Revenue: \$70.16B

EBITDA: \$6.61B

FCF: \$5.6B

Net Income: \$2.4B

## Risks

Valero Energy Corporation faces a plethora of risks including but not limited to: political, foreign exchange, regulatory environment, crude oil spread and macroeconomic risks. Although electric vehicles are becoming available and the push for renewable energy is active, hybrid and electric automobiles remain to be a minor component of the transportation sector. Therefore, demand for gasoline is not forecast to significantly decline within our investment timeline of 5-10 years. Spread divergence between WTI and Brent could also have a negative impact on both margins and as a competitive position perspective for Valero Energy.

## 5-Year Stock Performance



## Competitive Analysis

The petroleum refining industry contains high competition, high barriers to entry, and high regulation level. The four largest companies account for 56% of industry revenue in 2017, and Valero controls the second largest market share, of approximately 13%. Large companies dominate the market due to the high capital costs required to maintain refining plants. Valero's major competitors are Marathon Petroleum Corporation, Phillips 66, Andeavor, and Devon. Price is the main basis of competition in the industry, and Valero is able to provide competitive prices due to its leadership in input flexibility.

## Competitive Advantages

Valero Energy has a major competitive advantage in the refining space due to its ability to process 86 different varieties of crude allowing for increased margins and lower costs. This makes Valero the industry leader in input flexibility. Valero Energy strategically positioned its refineries in Texas where the majority of North American crude oil supplies exist. This allows for transportation costs to be reduced significantly. As a U.S. company, Valero is able to purchase WTI crude instead of the international benchmark of Brent, allowing for lower input costs per barrel of throughput compared to its international competitors.

## Corporate Social Responsibility

In 2016 the company generated more than \$41 million for charities or causes through direct donations, employees, and its charitable foundation. Employees also logged more than 140,000 community service hours. In 2016, for the third consecutive time, Valero was named one of America's 50 most community-minded major companies, the Civic 50; and was the leading energy company on the list. Valero's refineries have consistently been ranked among the top facilities in energy efficiency, in industry-wide surveys. The company plans to continue reducing its greenhouse-gas and other emissions through adoption of new technologies, and more efficient operations. From 2012 - 2015, the average per-barrel greenhouse-gas emission decreased by 15 percent from the previous four-year average.

