

Current Price: \$107.63

Target Price: **\$123.35**

Recommendation: **BUY**

(+14.61%)

Hess Corporation (HES)

Analyst: Duke Tran

April 6th, 2022

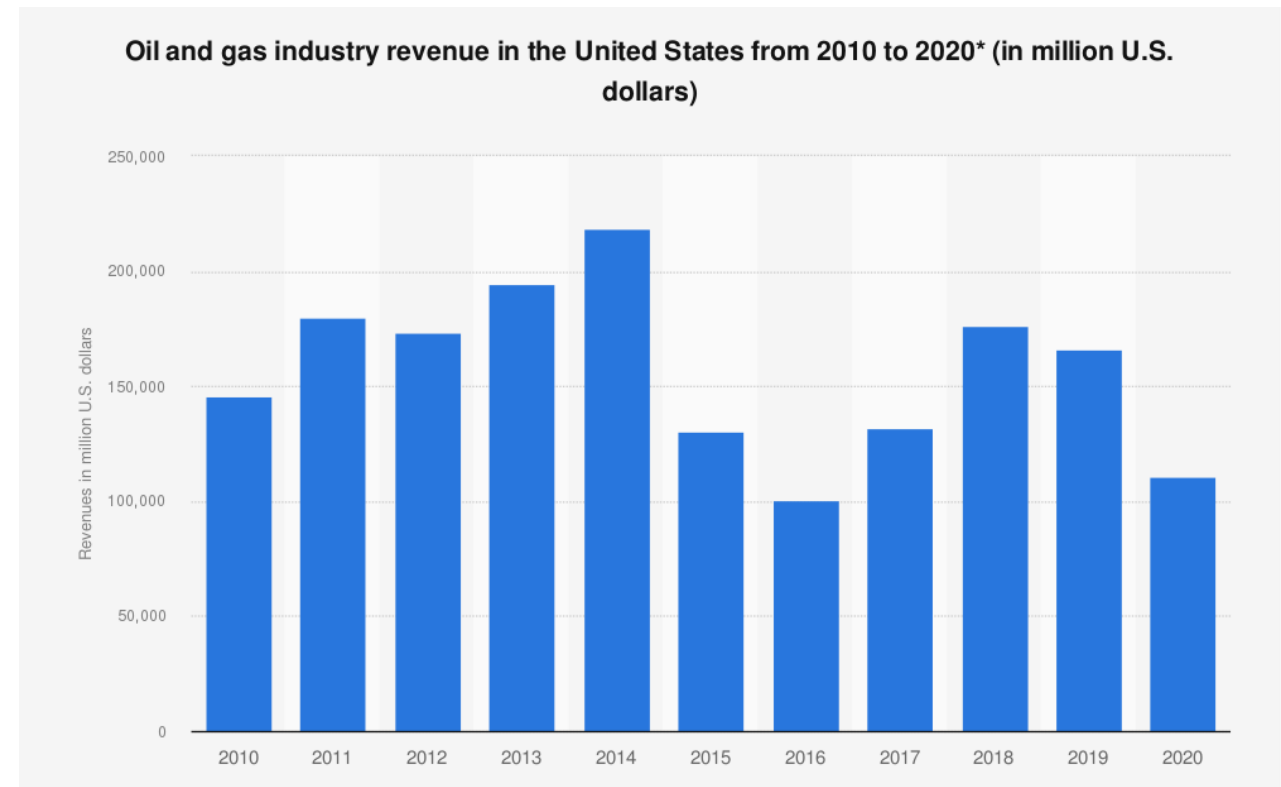
Overview

- Industry Overview
- Company Overview
- Management
- Competition
- Thesis 1
- Thesis 2
- Thesis 3
- Risks
- Valuation

Industry Overview

ENERGY SECTOR

- Companies that produce and supply energy
- Exploration and development of oil or gas reserves, oil or gas drilling, and refining
- Energy prices driven by global supply and demand for energy



Industry Overview

OIL & GAS INDUSTRY



- Upstream
 - Drilling, pumping, and production of oil and natural gas
 - Hess is an exploration and production (E&P) company
- Midstream
 - Processes, stores, and transports oil from production sites
 - Hess Midstream LP
- Downstream
 - Operate refineries to convert crude oil and natural gas to finished products
 - Sell to energy providers and gas stations

MARKET TRENDS

- Producers perform better when oil and gas prices are higher
- During the pandemic, crude oil prices dropped significantly
 - By early 2021, oil returned to pre-pandemic prices
 - Supply was slow to ramp up
- Russia-Ukraine conflict, crude oil and gasoline prices increasing
 - Pulled out of deals and ceased business with Russian producers
 - Organization of Petroleum Exporting Countries (OPEC) slow to urge increases in oil production

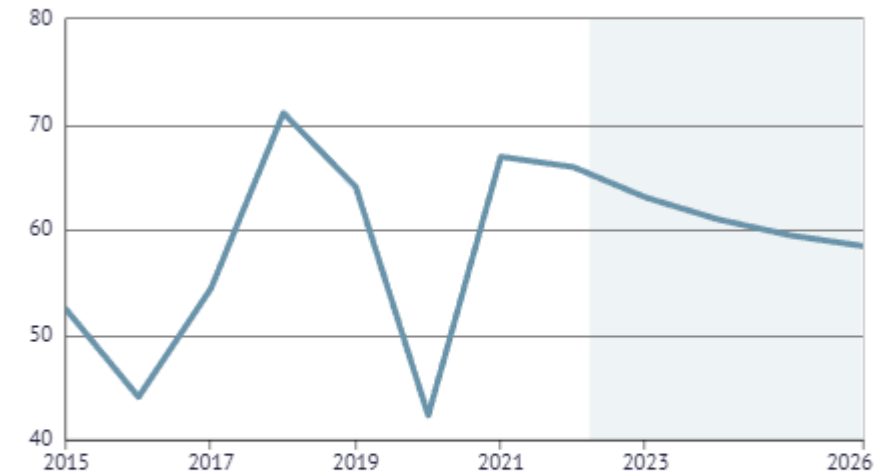
Industry Overview

KEY FIGURES



IMF: Brent Crude Oil Price Projection

US\$ per barrel

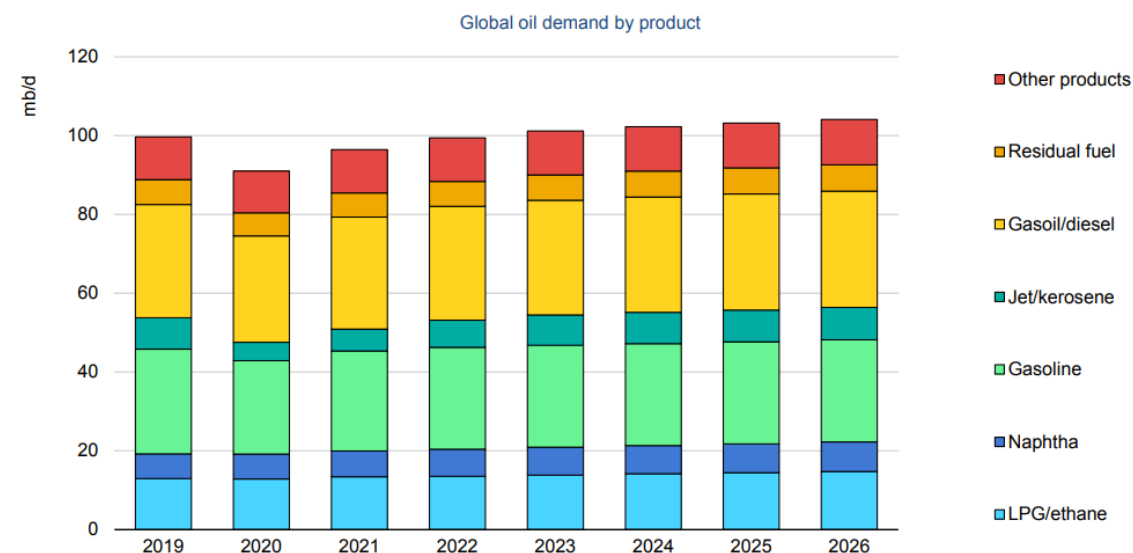
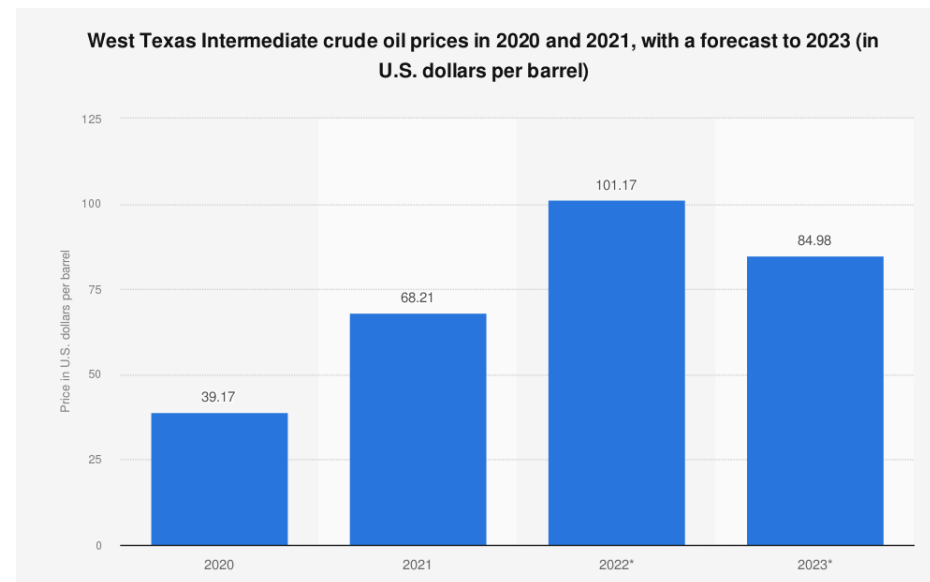


Year	2018	2019	2020	2021	2022	2023	2024	2025	2026
\$/bbl	1.07	64.03	42.30	66.91	65.93	63.04	60.95	59.43	58.42

Industry Overview

MARKET TRENDS

- 2022 – high crude oil prices, rampant volatility and fluctuations
 - Supply can't meet demand
- As production gradually increases, crude oil prices will continue to fluctuate
 - Prices should remain relatively high, probably through to 2023
- Global oil demand expected to surpass demand levels prior to pandemic



Company Overview

KEY FINANCIALS

Ticker: HES	Current Price: \$107.63	Market Cap: \$33.273 B
Sector: Energy	Target Price: \$123.35	Shares Outstanding: \$33.273 B
Industry: Oil & Gas E&P	52 Week Range: \$61.93 - \$109.23	Dividend Yield: 1.40%

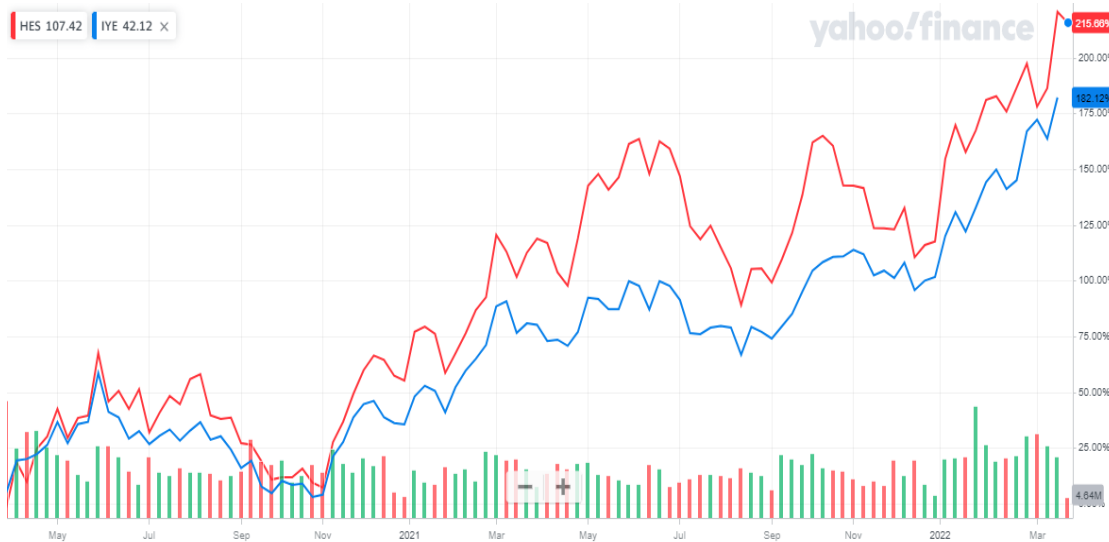
- Hess Corporation is an American exploration and production (E&P) company
- Focuses on exploration and production of crude oil, natural gas liquids (NGL), and natural gas
- Production operations in U.S., Guyana, the Malaysia/Thailand Joint Development Area (JDA), and Malaysia
 - Exploration activities primarily offshore from Guyana, secondarily in the Gulf of Mexico and offshore from Suriname and Canada

Company Overview

KEY FIGURES



HES has outperformed the energy ETF over 2 years



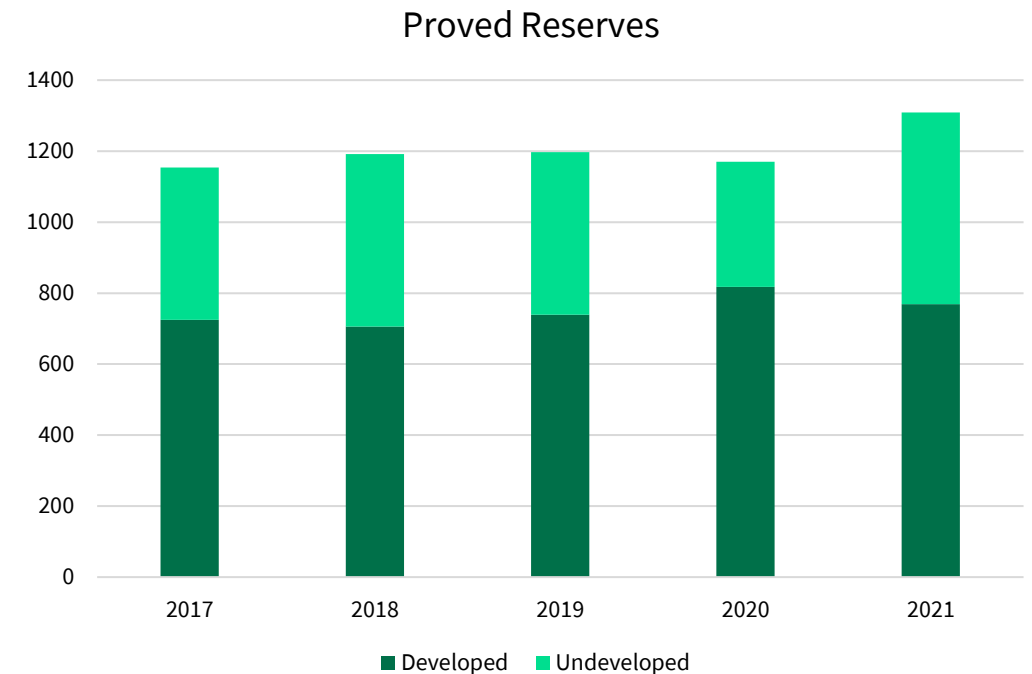
HES has outperformed EOG and tracked crude oil prices more closely over 2 years



Company Overview

INTRODUCTION

- Two segments: Upstream (E&P) and Midstream
- Total proved reserves: 1,309 million barrels of oil equivalent (as of 12/31/21)
 - Developed: 769 million
 - Undeveloped: 540 million
- Developed reserves can be expected to be recovered using existing wells, equipment, and operating methods
 - Cost of the required equipment is relatively minor
- Undeveloped reserves can be expected to be recovered from new wells on undrilled acreage or from existing wells
 - Require relatively major expenditures for recompletion



Company Overview

INTRODUCTION

- Mix of working interest (WI) with several companies
 - ExxonMobil, Equinor, and PETRONAS
- Working interest
 - Type of investment in oil and gas drilling operations
 - Liable for portion of ongoing costs associated with the exploration, drilling, and production
 - Share in the profits of production
 - Tax benefits associated with costs and losses
- Operating WI
 - Operator of the given province
 - Responsible for making all operational decisions such as selecting wells and determining drilling
- Non-operating WI
 - Not involved in daily operations, consulted on prior to major production decisions
 - Less costly, operator bears responsibility for most operating expenses
 - Receive less revenues in return

Company Overview

INTRODUCTION

Revenue Breakdown

Business Segment



● Natural Gas Liquids ● Natural Gas ● Crude Oil ● Other

- Crude Oil: 67.5%
- Natural Gas: 13.9%
- Natural Gas Liquids: 6.4%
- Other: 12.3%

Geographic Segment

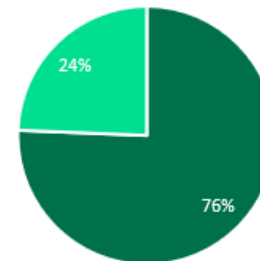


● Malaysia and JDA ● Guyana ● United States ● Other

- United States: 77.2%
- Malaysia and JDA: 10.9%
- Guyana: 7.5%
- Other: 4.3%

Segment Breakdown

Adjusted Net Income (FY2021)



■ Upstream ■ Midstream

- Upstream: \$888 million (76%)
- Midstream: \$286 million (24%)

Company Overview

UPSTREAM

- Hess is primarily known for its upstream segment
- Most E&P operations done within the U.S.
 - Bakken Shale Play in the Williston Basin of North Dakota
 - Offshore properties in the Gulf of Mexico
 - 30% interest in offshore Guyana with Stabroek Block
- Minor areas of interest
 - 50% WI in Block A-18 of the Malaysia/Thailand Joint Development Area (JDA) in the Gulf of Thailand
 - 50% WI in Block PM301 and Block PM302 located in the North Malay Basin (NMB) offshore from Peninsular Malaysia
 - 8% WI in several oil fields in Libya
 - 33% WI in Block 42 and Block 59 located offshore from Suriname
 - 25% WI in three exploration licenses offshore Newfoundland, Canada



Company Overview

MIDSTREAM

- Hess Midstream LP
 - Fee-based services such as gathering, compressing, and processing natural gas and fractionating natural gas liquids (NGL)
 - Services gathering, terminaling, loading, and transporting crude oil and NGL
 - Storing and terminaling propane and water handling
 - Bakken Shale Play in North Dakota
- Sizeable portfolio of assets
 - Tioga Gas Plant and Rail Terminal
 - Hawkeye Gas Facility and Oil Facility
 - Little Missouri 4 Gas Plant
- Hess has 43.5% ownership interest
 - Remainder owned by mutual funds and institutions
 - Some institutions with largest percentages of shares: CI Investments, Inc. (9.03%), Energy Income Partners LLC (7.02%), and Invesco Advisers, Inc. (6.21%)



Management



John B. Hess
CEO and Director

Over 40 years of experience in oil and gas industry



Gregory P. Hill
President and COO

25 years at Royal Dutch Shell in operations, engineering, technical, and managerial roles



John P. Rielly
Executive VP and CFO

Former Partner at Ernst & Young, LLP for 17 years



Gerbert Schoonman
Senior VP, Global Production

20 years with Royal Dutch Shell in operational and leadership roles

Competition



Marathon Oil Corporation (MRO)

- Exploration, production, and marketing of crude oil and condensate, natural gas liquids, and natural gas
- Portfolio consists of WI in Texas, the Bakken in North Dakota, Oklahoma, and the Permian in New Mexico



Coterra Energy Inc. (CTRA)

- Development, exploration and production of oil, natural gas, and natural gas liquids in the United States
- Focuses on the Marcellus Shale located in Susquehanna County, Pennsylvania



Diamondback Energy, Inc. (FANG)

- Acquisition, development, exploration, and exploitation of unconventional and onshore oil and natural gas reserves in the Permian Basin in West Texas
- Focuses on the development of the Spraberry and Wolfcamp formations of the Midland basin; and the Wolfcamp and Bone Spring formations of the Delaware basin



Continental Resources, Inc. (CLR)

- Explores for, develops, produces, and manages crude oil, natural gas, and related products
- Notable WI in the Bakken in North Dakota and Montana, the Anadarko Basin of Oklahoma, and the Permian Basin of Texas

INVESTMENT THESES



THESIS I

Hess's increasing financial strength will foster strong cash flow growth and capital returns



THESIS II

Investments in lucrative projects within key provinces will bolster growth and maintain low costs



THESIS III

Hess's portfolio is poised to deliver long-term value while incorporating measures for sustainability

Investment Thesis I

Hess's increasing financial strength will foster strong cash flow growth and capital returns.

- \$2.7 billion in cash (12/31/2021)
- Large focus on reducing debt levels
 - Used \$500 million during February 2022 to repay remainder of term loan
 - \$2.4 billion in near term debt maturities within next 10 years
 - Well poised to pay off debt while maintaining expectation of at least \$1 billion in cash
 - Increasing cash flow growth
- Expand cash margins by decreasing cash costs
 - Increasing efficiency of production
 - Profit more on operations through cost reductions and more effective extraction
 - Bring costs of \$12/BOE (barrel of oil equivalent) down to \$9/BOE within next 5 years

Investment Thesis I

Hess's increasing financial strength will foster strong cash flow growth and capital returns.

- Increase cash flow from operations

1) Limiting net capital expenditures

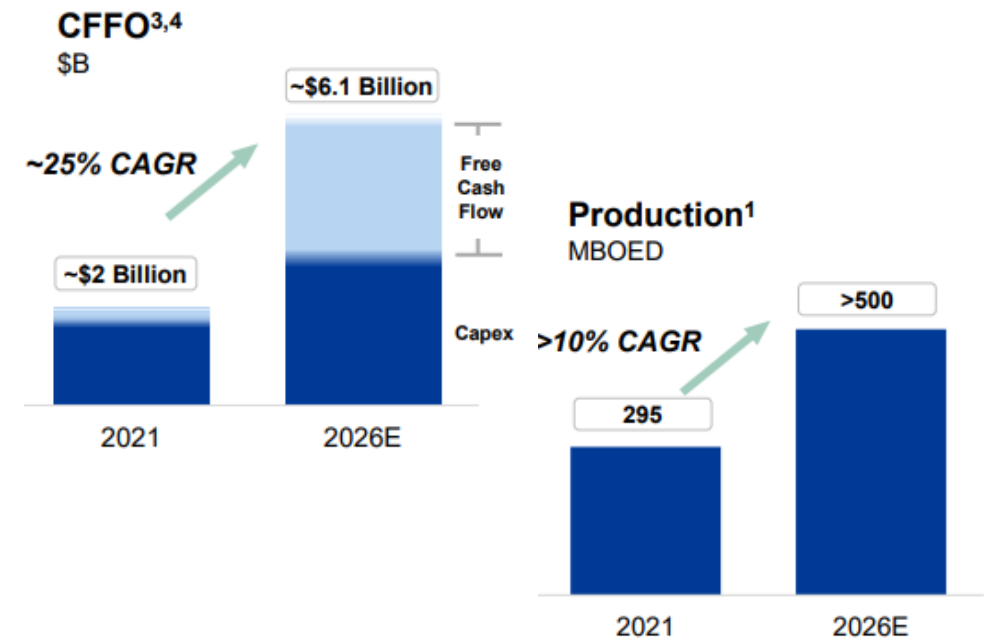
- Keep cash outflows low
- Total: \$1.15 billion in net capex in 2022 for the following reserves
 - JDA and North Malay Basin reserves: \$270 million
 - Gulf of Mexico: \$90 million
 - Bakken: \$790 million
- Compared to \$1.70 billion for E&P in 2021

2) Boosting production

- Investments in Guyana and the Stabroek Block
- Over 10% CAGR within next 5 years
- Production increase from 295 MBOED (thousand barrels oil equivalent per day) in 2021 to over 500 by 2026

- Both plans will contribute to **25% CAGR** goal in cash flow from operations

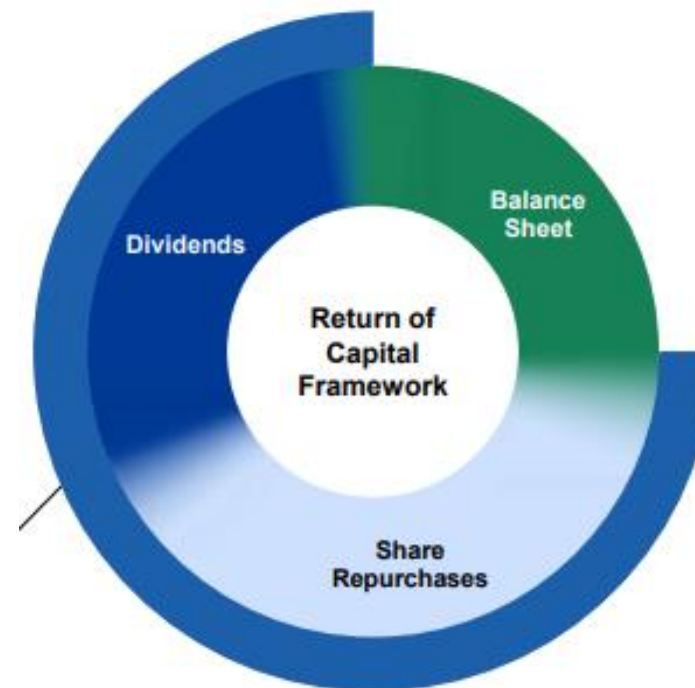
- Maintaining low capex
- Immense growth in free cash flow



Investment Thesis I

Hess's increasing financial strength will foster strong cash flow growth and capital returns.

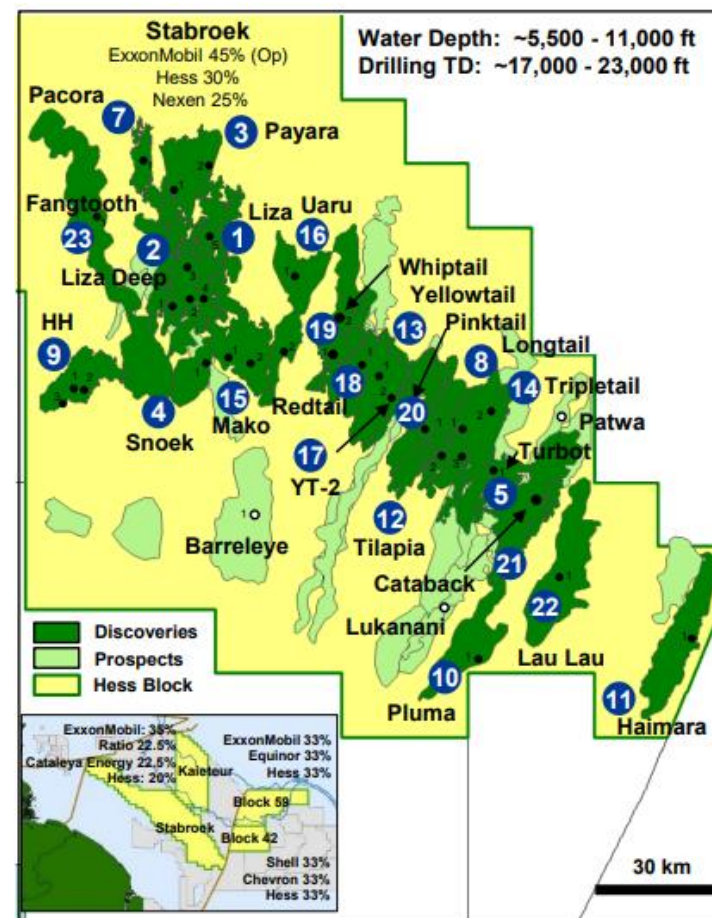
- Committed to increasing capital returns
 - Up to 75% of annual free cash flow to be used to increase dividends and repurchase shares
 - Greatly benefit shareholders while not impacting core business nor financial health
 - Already increased the regular dividend by 50% on March 1, 2022 and plan on continuing to increase it
 - Accelerate share repurchases as free cash flow grows, especially with high oil prices



Investment Thesis II

Investments in lucrative projects within key provinces will bolster growth and maintain low costs.

- Stabroek Block in Guyana
 - 30% working interest
 - Operator is ExxonMobil (ExxonMobil has 45%, Nexen has 25%)
 - Province occupies 6.6 million acres, low entry cost
 - 23 major discoveries to date, over 10 BBOE (billions barrels of oil equivalent)
 - Yields potential for up to 10 FPSOs (floating production, storage, and offloading vessel)
 - Sanctioned projects have breakeven oil price of \$25-\$35/BBL
 - Takes less than half the drilling time and cost to produce here compared to typical offshore deepwater provinces
 - Low royalties
 - Favorable contractual terms established with Georgetown, the capital of Guyana
 - Exceptional reservoir quality, low development costs



Investment Thesis II

Investments in lucrative projects within key provinces will bolster growth and maintain low costs.

- Liza Phase 1
 - Began producing oil in December 2019 using Liza Destiny FPSO at 120,000 gross BOPD (barrels of oil per day)
 - \$35/BBL breakeven
 - Reduced gross development costs from \$4.4 billion to \$3.5 billion
 - Optimizing the production capacity of the Liza Destiny this year
 - Increase to over 140,000 gross BOPD
- Liza Phase 2
 - Began producing oil in February 2022 using Liza Unity FPSO at 220,000 gross BOPD
 - Ramping up Liza Phase 2 production throughout the year following slowdown in production the previous year

Liza Phase 1: Destiny

Discovered in 2015
First oil achieved 2019



Liza Phase 2: Unity

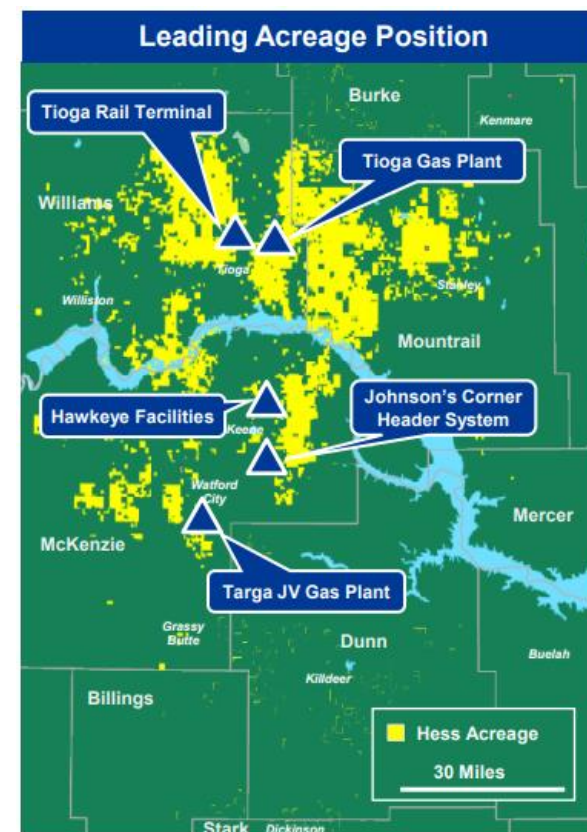
Discovered in 2015
First oil achieved 2022



Investment Thesis II

Investments in lucrative projects within key provinces will bolster growth and maintain low costs.

- Bakken Shale Play
 - 75% WI as an operator, occupying about 460,000 net acres
 - Other companies retaining the remaining 25%
 - Continental Resources
 - ExxonMobil
 - Whiting Petroleum
 - EOG Resources
 - Projected to yield 160-165 MBOED through 2022
 - D&C (drilling and completion) costs forecasted to remain at \$5.8 million per well, consistent with 2021
 - Lean principles to optimize infrastructure, seeking to maximize cash flow
 - Hess Midstream facilities located within the play
 - Leverage advantaged midstream infrastructure to support upstream growth



Investment Thesis III

Hess's portfolio is poised to deliver long-term value while incorporating measures for sustainability.

- Structuring portfolio to provide value through the long-term
 - All assets will generate positive free cash flow starting in 2022
 - Generating high returns and planning to invest in up to 10 FPSOs to develop over 10 BBOE of gross discovered resources in Guyana
 - Petroleum is a sweet crude oil (low sulfur content and reduced carbon intensity)
 - Help in reducing the global carbon footprint by selling a less-carbon-intensive oil
 - Optimize infrastructure and cash flow generation in Bakken
 - Reach 200 MBOED net production by 2024
 - \$3 billion of free cash flow in 2026 altogether
 - Breakeven of \$45/BBL by 2026
 - Expanding cash margins, reducing portfolio cash costs

Investment Thesis III

Hess's portfolio is poised to deliver long-term value while incorporating measures for sustainability.

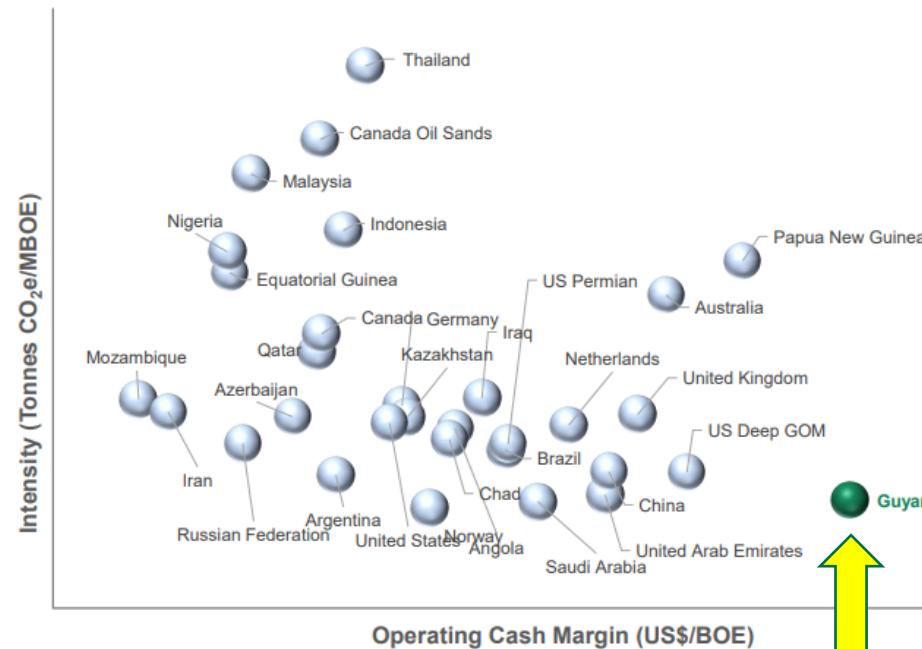
- Committed to reducing emissions while keeping up with growth targets
 - Support the Paris Agreement and goal of achieving net zero emissions by 2050
 - Outperformed emission reduction target for 2020, reduced operated GHG emissions intensity by 46% in 2020 compared to 25% target vs. 2014
 - Reduce operated GHG emissions intensity by 50% vs. 2017 by 2025
 - Reduce methane emissions intensity by 50% vs. 2017 by 2025
 - Outperformed flaring intensity target by 59% compared to 50% target vs. 2014
 - Zero routine gas flaring (production flaring) by 2025
 - Disposing of large unwanted amounts of associated petroleum gas (APG) during crude oil extraction
- Contributed \$12.5 million to the Salk Institute's Harnessing Plants Initiative (HPI)
 - Enhance plants' natural ability to store carbon and mitigate effects of climate change
 - Advancing two primary projects
 - CRoPS (CO₂ Removal on a Planetary Scale) Program
 - Coastal Plant Restoration (CPR) Program
 - Build on Salk discovery of a crucial gene
 - Research and develop plants capable of storing billions of tons of atmospheric carbon per year (plant-based carbon capture and storage)

Investment Thesis III

Hess's portfolio is poised to deliver long-term value while incorporating measures for sustainability.

With their projects in Guyana, Hess is also poised to benefit in both long-term value and sustainability. Guyana offers the highest operating cash margin and production growth potential globally while maintaining low emissions intensity.

Operating Cash Margin vs. Scope 1+2 Emissions Intensity



2021-25 Production CAGR (BOE) Top 15



Risks

GLOBAL ENVIRONMENT/PRICE RISK

- Operations and cash flows highly dependent on market prices
- Market can be volatile
- Russia-Ukraine conflict - crude oil prices extremely sensitive, fluctuations in response to global developments

ALTERNATIVE ENERGY

- Increasing concern towards climate change and human effects on environment
- Sustainability initiatives may require significant operational changes and expenditures
- Impact returns and cash flow growth
- Reduce demand for crude oil and natural gas products
- Hurt revenues in the long run

GOVERNMENT REGULATIONS

- Business in numerous foreign countries and localities
- Subject to changing laws and regulations
- Political instability in developing oil and gas markets

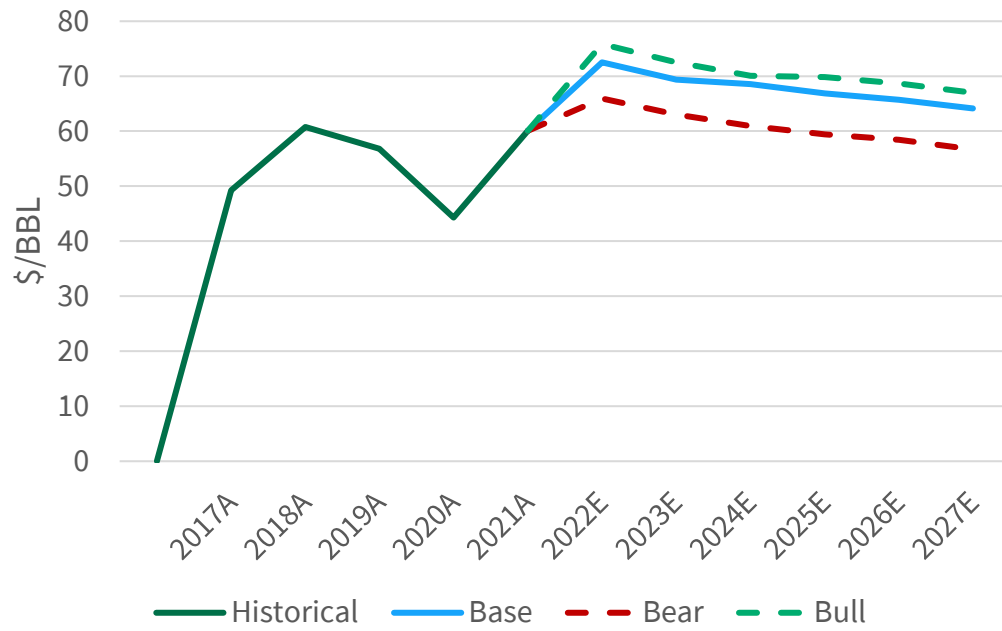
COVID-19

- Less likely to be realized
- If a stronger variant emerges or virus resurges
- Another shutdown could be disastrous for O&G industry
- Less travel, less demand for oil and natural gas

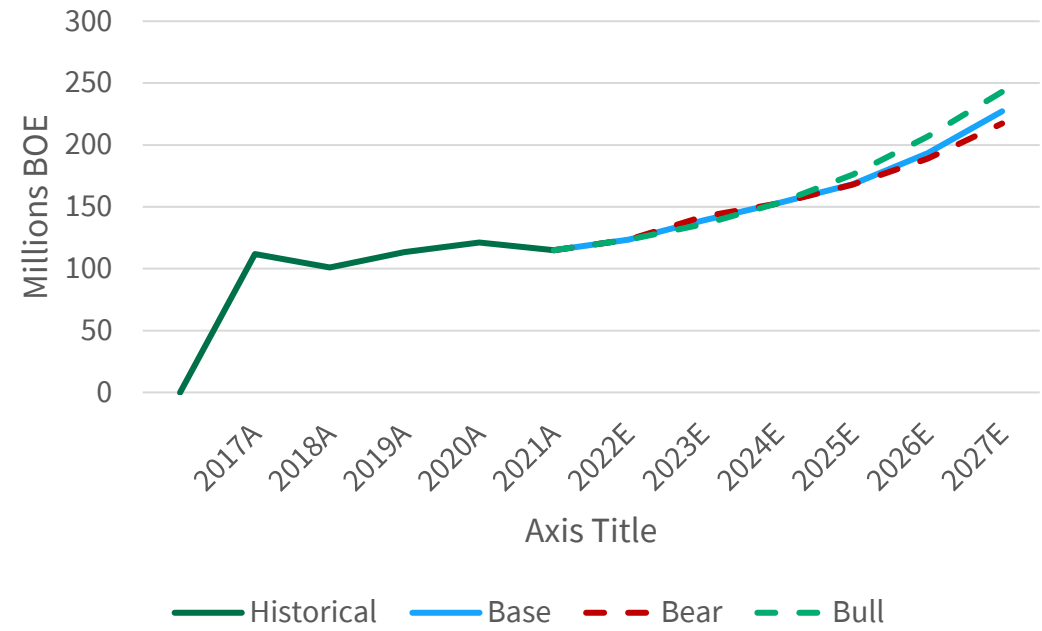
Valuation



Crude Oil Price



Crude Oil Production



Valuation



RELATIVE VALUATION

- Many upstream-focused oil and gas companies
- 6 companies, their business derived from E&P
- Good comparables, regularly compete for provinces, lease contracts, and oil reservoirs

BEAR CASE

- Revenue growth decline in future years
- Lessening demand for oil and gas, both as oil production and prices return to “normal” levels
- Prospect of being unable to capitalize on investment projects to reduce exploration/drilling and property impairment costs

BASE CASE

- More conservative approach, limited optimism for the near future
- Expected working capital to increase modestly, fell just short of expectations of maximizing cash flow and reducing costs
- Reduced net interest expense by 5% YoY to account for gradual paying off debts

BULL CASE

- Assumed nearing (but not exceeding) of targets for cash flow growth through reductions in operating costs
- Healthy increase YoY in total working capital as a result of cash accumulation and debt paydown

DCF Valuation	Weight	Premium
Bear Case	20%	-25.48%
Base Case	55%	20.55%
Bull Case	20%	55.46%
Relative Valuation	5%	-53.81%
Weighted Premium		14.61%

Stock Price Analysis	
Current Stock Price	107.63
Calculated Premium	14.61%
Target Price	\$123.35

- Investment Horizon: 6-18 months depending on progress on goals (especially production)
- Drivers of short to mid-term growth: increase in production, increasing demand, elevated prices
- Per Risks:
 - Regulations/Restrictions (specifically environmental): depends on magnitude, difficult due to bureaucracy, lengthy timeframes, lobbying, economic concerns, sector risk
 - Foreign Exposure (and nationalization): unlikely in areas where Hess has WI since they rely on O&G revenues for economic growth
- Per Relative Valuation: Hess may seem quite overvalued due to its P/E ratio, but my stance is that the stock is priced in for future earnings, check valuation for future P/E ratios
- Per Revenue Projections: originally based off analyst estimates and projections through to 2024, revised to incorporate forecasted crude oil prices and increased oil production by Hess

CLOSING REMARKS



SUMMARY

- Greatly outperformed the energy ETF, capitalized well off historical rise in oil prices
- Kept pace with the likes of EOG, even outperforming at times
- Strong financials (and emphasis on strengthening for the future), aiming for **cash flow growth** and **production increase**
- Guyana will prove to be lucrative and advantageous
- Providing **long-term value** while incorporating **sustainability**



THANK YOU

Questions?



Appendix

GLOBAL ENERGY CONSUMPTION

Figure 1.1 Primary Energy Overview
 (Quadrillion Btu)

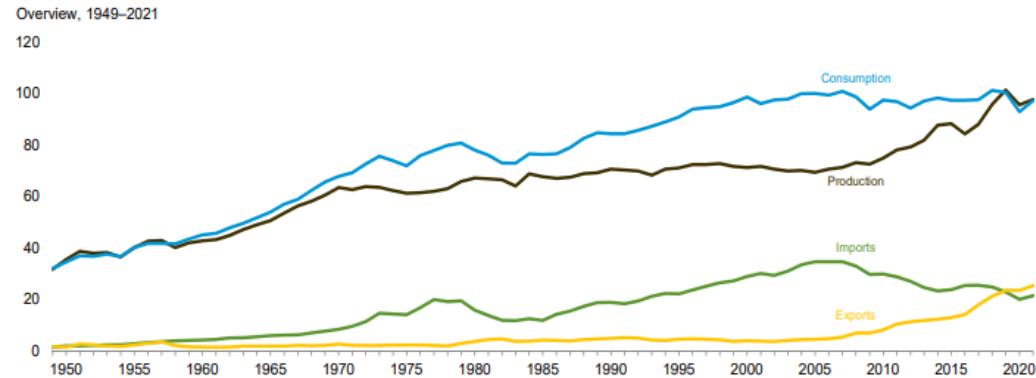
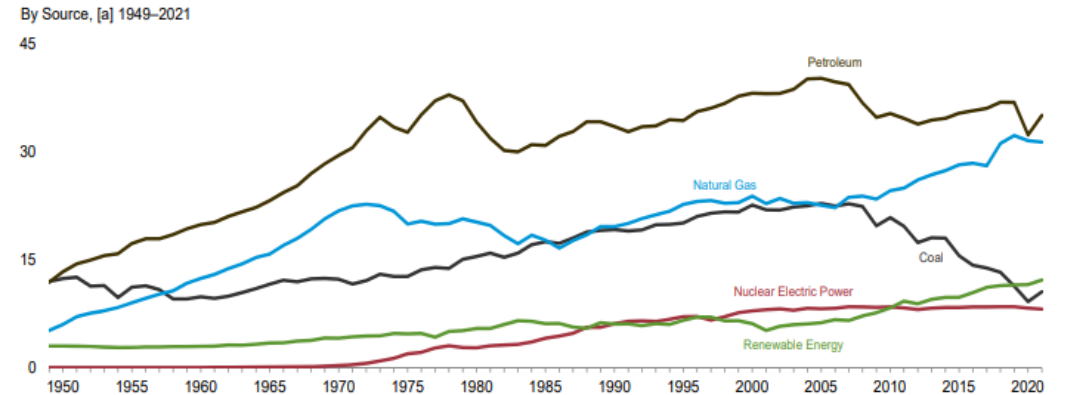


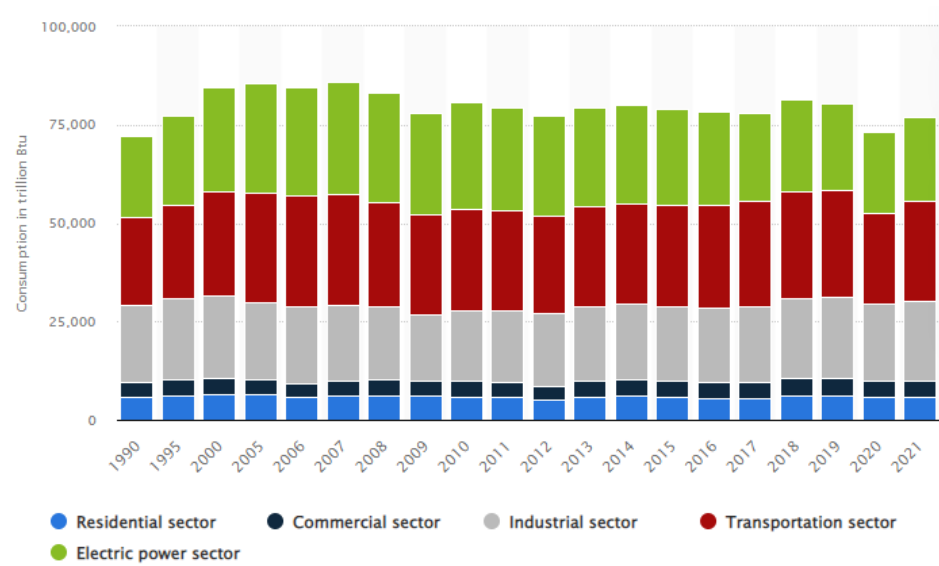
Figure 1.3 Primary Energy Consumption
 (Quadrillion Btu)



Appendix

FOSSIL FUELS

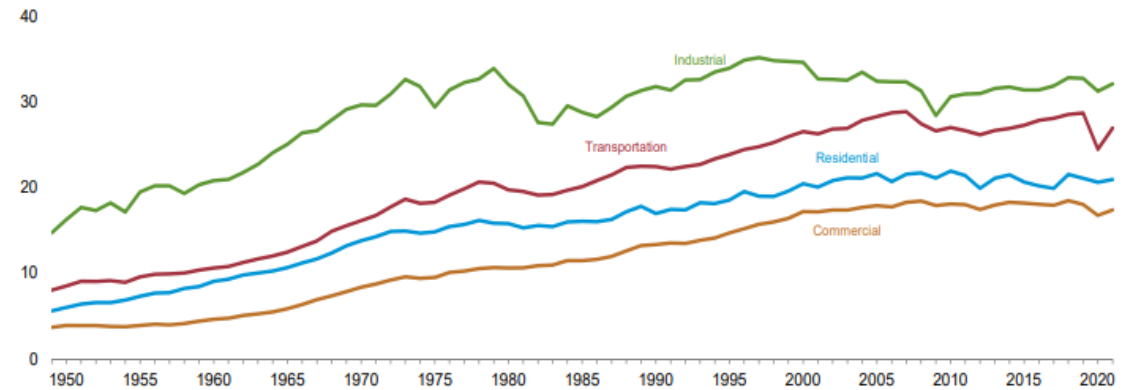
U.S.



Global

Figure 2.1 Energy Consumption by Sector
 (Quadrillion Btu)

Total Consumption by End-Use Sector, 1949–2021



Appendix

CONTRACTUAL OBLIGATIONS

	Payments Due by Period (in millions \$)				
	Total	2022	2023 and 2024	2025 and 2026	Thereafter
Capital expenditures	3,263	1,028	1,458	777	-
Operating expenses	180	132	42	6	-
Transportation and related contracts	2,574	390	639	453	1,092