

Valero Energy Corp. (VLO)

\$63.35 (As of 04/30/20)

Price Target (6-12 Months): **\$67.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 04/14/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: A

Momentum: F

Summary

Valero is poised to benefit from the new standard set by International Maritime Organization. The company being a producer of a significant amount of distillate fuel, will capitalize on this. Importantly, it has completed the Pasadena terminal project, which will boost export flexibility. Notably, the company beat first-quarter earnings estimates thanks to strong renewable diesel sales volumes. The firm has also been returning funds to its shareholders on a regular basis. However, Valero's cash and cash equivalents of \$1.5 billion is much lower than its total debt of \$11.5 billion, reflecting balance sheet weakness. Moreover, the coronavirus-induced lockdowns destroyed demand for the company's refined products. Notably, it has decided to defer some capital projects planned for 2020. As such, the stock warrants a cautious stance.

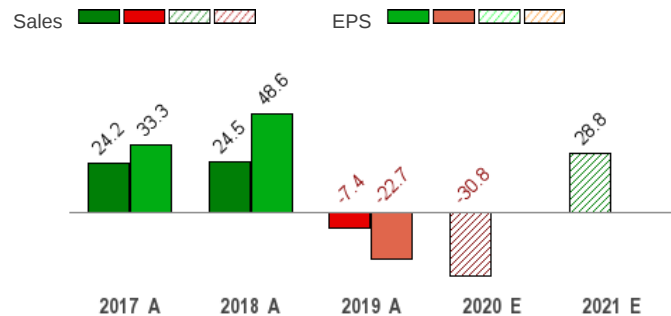
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$101.99 - \$31.00
20 Day Average Volume (sh)	5,498,114
Market Cap	\$25.9 B
YTD Price Change	-32.4%
Beta	1.96
Dividend / Div Yld	\$3.92 / 6.2%
Industry	Oil and Gas - Refining and Marketing
Zacks Industry Rank	Bottom 32% (171 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	326.7%
Last Sales Surprise	5.6%
EPS F1 Est- 4 week change	-155.4%
Expected Report Date	07/23/2020
Earnings ESP	0.0%
P/E TTM	11.6
P/E F1	NA
PEG F1	NA
P/S TTM	0.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	22,720 E	25,933 E	26,746 E	28,703 E	96,542 E
2020	22,102 A	15,719 E	17,839 E	22,761 E	74,963 E
2019	24,263 A	28,933 A	27,249 A	27,879 A	108,324 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.13 E	\$1.04 E	\$1.67 E	\$0.73 E	\$3.41 E
2020	\$0.34 A	-\$1.48 E	-\$0.45 E	-\$0.18 E	-\$1.93 E
2019	\$0.34 A	\$1.51 A	\$1.48 A	\$2.13 A	\$5.70 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/30/2020. The reports text is as of 05/01/2020.

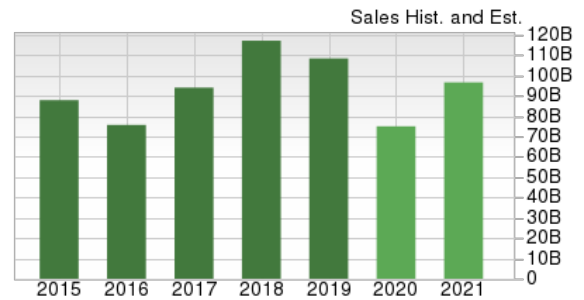
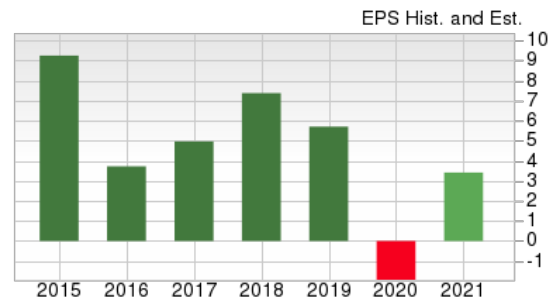
Overview

San Antonio, TX-based Valero Energy Corporation is the largest independent refiner and marketer of petroleum products in the United States. The company was founded in 1980. It has a refining capacity of 3.1 million barrels per day across 15 refineries located throughout the United States, Canada and the United Kingdom.

Moreover, Valero is a leading ethanol producer with 14 ethanol plants in the Midwest that have a combined capacity of 1.73 billion gallons per year. The products of the company are sold in the markets of the United States, Canada, the United Kingdom, Ireland and Latin America. The company's brand names are carried by around 7,000 outlets.

The company organizes its business through three reportable segments, namely, Refining, Ethanol and Renewable Diesel.

- **Refining:** The Refining segment was responsible for 84% of the total margin in 2019. It includes refining operations, wholesale marketing, product supply and distribution, and transportation operations. This segment is segregated geographically into the Gulf Coast, mid-continent, West Coast and Northeast regions.
- **Ethanol:** The Ethanol segment includes sales of internally produced ethanol and distillers grains. Operations of this segment are geographically located in the Central Plains region of the United States. This segment was responsible for less than 1% of the total margin in 2019.
- **Renewable Diesel:** In the first quarter of 2019, the company created this segment. The Renewable Diesel segment incorporates the operations of a consolidated joint venture, Diamond Green Diesel. Notably, the renewable diesel plant is North America's largest biomass-based diesel plant and it is located in Norco, LA. The segment provided 15% of the total margin in 2019, which was supported by the expansion of the Diamond Green Diesel plant.



Reasons To Buy:

- ▲ Among all the independent refiners, Valero offers the most diversified refinery base with a capacity of 3.1 million barrels per day in its 15 refineries located throughout the United States, Canada and the Caribbean. More importantly, Valero is best placed to reap profits from solid refining margins, mainly owing to its strategic refinery structure that enables it to use cheaper oil for more than half of its needs.
 - ▲ Valero has been returning funds to its shareholders on a regular basis. Through first-quarter 2020, the company returned \$548 million to its shareholders, of which \$147 million was used to repurchase around 2.1 million shares of common stock and \$401 million was paid as dividends to its shareholders. Notably, Valero reduced its capital expenditure view for 2020 by \$400 million to \$2.1 billion.
 - ▲ Majority of the company's refining plants are located at the Gulf coast area from where there is an easy access to the export facilities. This Gulf coast presence helped Valero expand its export volumes over the last few years and gain from high distillate margins. Additionally, in first-quarter 2020, the company completed the Pasadena terminal project, which will likely expand the product logistics portfolio, enhance capacity for biofuels blending and boost export flexibility.
 - ▲ Moreover, Valero is poised to benefit from the new standard set by International Maritime Organization (IMO). Per the standard, which was effective since January 2020, the proportion of sulfur in marine fuel has declined to 0.5% from the current 3.5%, thereby boosting demand for distillate fuel. Valero, being a producer of a significant amount of distillate fuel, is expected to capitalize on this.
 - ▲ Once the coronavirus pandemic gets under control, the company is projected to benefit from export volumes of refined petroleum products. This is because Valero has majority of its refining facilities in the U.S. Gulf Coast region. Notably, the company entered into long-term accords to utilize three new refined product terminals in Mexico. The leading refining player will be able to expand its product supply chain once the Guadalajara, Monterrey and Altamira terminals commence operations in 2021.
-

Among all the independent refiners, Valero offers the most diversified refinery base.

Reasons To Sell:

- ▼ In a bid to lower greenhouse gas emissions, Energy Information Administration (EPA) set a Renewable Fuel Standard. Per the new mandate, refiners need to add year-over-year higher volumes of advanced biofuels to gasoline. Following this, Valero is compelled to divert cash to ensure regulatory compliance, which can limit profitability. This is also likely to lead to the refiner incurring higher biofuel blending costs this year.
- ▼ The current market uncertainty caused by coronavirus-induced lockdowns and travel bans has reduced demand for the company's products like gasoline and jet fuel. Weak energy demand environment affected the company's first-quarter results and will continue to do so until the economies go into a recovery mode.
- ▼ Weak refining throughput volumes are affecting the company's refining segment, its biggest business unit. Also, lower ethanol prices and higher corn prices are hurting its ethanol segment's profit levels. Given the current market uncertainty, the situation is not expected to improve anytime soon.
- ▼ At the end of the first quarter, the company had cash and cash equivalents of \$1.5 billion, reflecting a decline from the fourth-quarter 2019 level of \$2.6 billion. However, total debt increased to \$11.5 billion, depicting a rise from \$9.7 billion in fourth-quarter 2019. Moreover, the company's interest coverage ratio of 2.92 compares unfavorably with the industry's 11.5. Given the weakness in energy demand, the company's profits will remain under pressure, which might pose difficulty for it in paying down the debt burden..
- ▼ The company has also decided to defer some capital projects, associated to its refining and ethanol segments, which were planned for this year.

The firm's weak refining business is concerning.

Last Earnings Report

Valero Beats Q1 Earnings on Renewable Diesel Sales Volumes

Valero Energy Corporation reported first-quarter 2020 earnings of 34 cents per share against the Zacks Consensus Estimate of a loss of 15 cents. However, quarterly earnings decreased from the year-ago earnings of 43 cents per share.

Total revenues fell from \$24,263 million in the prior-year period to \$22,102 million in the quarter under review. However, the top line surpassed the Zacks Consensus Estimate of \$21,617 million.

The better-than-expected results can be attributed to a rise in renewable diesel sales volumes and lower operating expenses. This was partially offset by lower ethanol prices and refining margin, as well as increased corn prices.

In first-quarter 2020, the company completed the Pasadena terminal project, which will likely expand the product logistics portfolio, enhance capacity for biofuels blending and boost export flexibility.

Segmental Performance

Operating loss from the **Refining** segment was reported at \$2,087 million against operating income of \$479 million in the year-ago quarter. The Zacks Consensus Estimate for the same was pegged at a profit of \$813 million. Refining throughput volumes marginally declined from first-quarter 2019.

In the **Ethanol** segment, the company reported operating loss of \$197 million against a profit of \$3 million in the year-ago quarter. Moreover, the reported figure was wider than the Zacks Consensus Estimate of a loss of \$55 million. The downside was caused by lower ethanol prices and increased corn prices. Ethanol production volumes in the quarter were reported at 4.1 million gallons per day.

Valero created a new segment in first-quarter 2019, namely **Renewable Diesel**, which incorporated the operations of a consolidated joint venture, Diamond Green Diesel. Operating income from the segment was \$198 million compared with \$49 million in the year-ago period. The figure surpassed the Zacks Consensus Estimate of \$104 million. The increase was attributed to a rise in renewable diesel sales volumes.

Expenses & Operating Income

General and administrative expenses in the Corporate and other segment totaled \$177 million compared with the prior-year level of \$209 million. Operating expenses fell to \$1,124 million from the year-ago figure of \$1,215 million. Total cost of sales rose to \$24,187 million in the quarter from the year-ago period's \$23,730 million.

Quarterly operating loss in the quarter was \$2,277 million against operating income of \$308 million in the year-ago period.

Throughput Volumes

During the quarter, refining throughput volumes were 2,824 thousand barrels per day (Mbpd), marginally down from the prior-year quarter's 2,865 Mbpd.

In terms of feedstock composition, sweet crude, medium/light sour crude and heavy sour crude accounted for 54.5%, 8.9% and 12.8%, respectively, of its total volume. The remaining volumes came from residuals, other feedstock blendstocks and others.

The Gulf Coast contributed approximately 59.1% to total throughput volume. Mid-Continent, North Atlantic and West Coast regions accounted for 15.3%, 17.2% and 8.4%, respectively, of the total throughput volume.

Throughput Margins

Refining margin per barrel of throughput decreased to \$7.24 from the year-ago level of \$8.00. Refining operating expense per barrel was \$3.87 compared with \$4.15 in the year-ago quarter. Depreciation and amortization expenses increased to \$2.09 a barrel from \$1.96 in the prior-year quarter. As such, adjusted refining operating income was recorded at \$1.28 per barrel of throughput, lower than the year-ago level of \$1.89.

Share Repurchase

Valero returned \$548 million to shareholders, of which \$147 million was used to repurchase 2.1 million shares of common stock and \$401 million was paid as dividends to shareholders.

Capital Expenditure & Balance Sheet

First-quarter capital expenditure totaled \$705 million, of which \$468 million was allotted for sustaining the business.

At the end of the quarter, the company had cash and cash equivalents of \$1.5 billion, reflecting a decline from the fourth-quarter 2019 level of \$2.6 billion. As of Mar 31, 2020, it had a total debt of \$11.5 billion, depicting a rise from \$9.7 billion in fourth-quarter 2019. Its debt-to-capitalization was 34%. The company entered into a revolving credit facility worth \$875 million on Apr 13.

Outlook

Valero expects capital expenditure for 2020 to be \$2.1 billion, which is \$400 million lower than the original guidance. The St. Charles alkylation unit is expected to come online in 2020. Moreover, the company's Diamond Green Diesel expansion project and Diamond Pipeline expansion are scheduled to be completed in 2021.

The current market uncertainty caused by coronavirus-induced lockdowns and travel bans has reduced demand for the company's products like

Quarter Ending **03/2020**

Report Date	Apr 29, 2020
Sales Surprise	5.63%
EPS Surprise	326.67%
Quarterly EPS	0.34
Annual EPS (TTM)	5.46

gasoline and jet fuel. Weak energy demand environment affected the company's first-quarter results and will continue to do so until the economies go into a recovery mode.

Valuation

Valero shares are down 32.3% in the year-to-date period, and 28.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and Zacks Oils-Energy sector are down 38.7% and 37.8%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and sector are down 33.9% and 41.2%, respectively.

The S&P 500 index is down 8.8% in the year-to-date period, but up 0.5% in the past year.

The stock is currently trading at 68.24X forward 12-month Price/Earnings, which compares to 76.18X for the Zacks sub-industry, 56.72X for the Zacks sector and 20.80X for the S&P 500 index.

Over the past five years, the stock has traded as high as 73.36X and as low as 4.6X, with a 5-year median of 10.62X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$68 price target reflects 73.25X F12M earnings.

The table below shows summary valuation data for VLO.

Valuation Multiples - VLO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	68.24	76.18	56.72	20.8
	5-Year High	73.36	76.18	56.72	20.8
	5-Year Low	4.6	8.02	11.25	15.19
	5-Year Median	10.62	11.12	18.43	17.44
EV/EBITDA TTM	Current	5.17	5.82	4	10.66
	5-Year High	15.52	16.47	10.41	12.87
	5-Year Low	2.03	4.3	3.06	8.27
	5-Year Median	6.92	7.39	6.53	10.78
P/B TTM	Current	1.15	0.74	0.8	3.89
	5-Year High	2.34	1.83	1.62	4.55
	5-Year Low	0.59	0.42	0.51	2.84
	5-Year Median	1.48	1.26	1.32	3.64

As of 04/30/2020

Industry Analysis Zacks Industry Rank: Bottom 32% (171 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
BP p.l.c. (BP)	Neutral	3
Delek US Holdings, Inc. (DK)	Neutral	3
Marathon Petroleum Corporation (MPC)	Neutral	3
PBF Energy Inc. (PBF)	Neutral	3
Royal Dutch Shell PLC (RDSA)	Neutral	3
Chevron Corporation (CVX)	Underperform	5
HollyFrontier Corporation (HFC)	Underperform	5
Phillips 66 (PSX)	Underperform	5

Industry Comparison Industry: Oil And Gas - Refining And Marketing				Industry Peers		
	VLO	X Industry	S&P 500	MPC	PBF	PSX
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Underperform
Zacks Rank (Short Term)	3	-	-	3	3	5
VGM Score	B	-	-	C	A	B
Market Cap	25.93 B	1.37 B	20.61 B	20.84 B	1.37 B	32.15 B
# of Analysts	9	5	14	9	7	9
Dividend Yield	6.19%	0.00%	2.11%	7.23%	0.00%	4.92%
Value Score	B	-	-	C	A	B
Cash/Price	0.12	0.15	0.06	0.09	0.90	0.06
EV/EBITDA	5.25	4.56	11.87	6.16	2.62	6.96
PEG Ratio	NA	4.38	2.47	NA	NA	4.58
Price/Book (P/B)	1.15	0.94	2.67	0.49	0.38	1.20
Price/Cash Flow (P/CF)	5.62	4.71	10.66	3.00	2.45	6.48
P/E (F1)	NA	20.45	19.01	NA	NA	25.22
Price/Sales (P/S)	0.24	0.23	2.10	0.17	0.06	0.29
Earnings Yield	-3.05%	-0.09%	5.05%	-6.30%	-46.32%	3.96%
Debt/Equity	0.41	0.62	0.72	0.71	0.64	0.41
Cash Flow (\$/share)	11.28	4.65	7.01	10.70	4.65	11.30
Growth Score	A	-	-	B	A	B
Hist. EPS Growth (3-5 yrs)	-5.36%	11.57%	10.88%	4.56%	-11.97%	12.36%
Proj. EPS Growth (F1/F0)	-133.90%	-64.40%	-7.32%	-140.82%	-686.82%	-63.96%
Curr. Cash Flow Growth	-11.67%	2.05%	5.92%	13.40%	-27.27%	-27.54%
Hist. Cash Flow Growth (3-5 yrs)	-2.48%	10.33%	8.55%	12.38%	-2.24%	0.90%
Current Ratio	1.44	1.29	1.23	1.25	1.52	1.24
Debt/Capital	28.94%	39.06%	43.84%	42.36%	39.06%	29.22%
Net Margin	0.41%	1.69%	11.08%	2.11%	1.30%	2.81%
Return on Equity	10.24%	10.26%	16.44%	7.45%	3.17%	13.51%
Sales/Assets	2.03	1.63	0.54	1.28	2.72	1.88
Proj. Sales Growth (F1/F0)	-30.80%	-15.40%	-1.42%	-26.67%	-15.60%	-30.37%
Momentum Score	F	-	-	F	F	F
Daily Price Chg	-4.42%	-0.45%	-2.39%	-2.91%	2.24%	-0.45%
1 Week Price Chg	1.43%	1.68%	-1.74%	1.22%	-0.92%	1.68%
4 Week Price Chg	52.65%	41.47%	17.07%	51.18%	93.55%	41.47%
12 Week Price Chg	-23.92%	-26.66%	-18.53%	-42.16%	-56.85%	-18.90%
52 Week Price Chg	-28.22%	-30.23%	-9.82%	-45.34%	-65.49%	-17.88%
20 Day Average Volume	5,498,114	1,165,524	2,641,413	11,554,530	4,672,628	3,960,093
(F1) EPS Est 1 week change	-235.07%	-18.77%	0.00%	-34.35%	-37.08%	-18.77%
(F1) EPS Est 4 week change	-155.42%	-57.97%	-6.62%	-205.77%	-728.92%	-40.90%
(F1) EPS Est 12 week change	-120.99%	-70.44%	-13.28%	-129.60%	-217.81%	-70.44%
(Q1) EPS Est Mthly Chg	-12,585.70%	-89.19%	-11.97%	-589.01%	-61.18%	-90.85%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	A
Momentum Score	F
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.