The Fox Fund
Temple University Student Fund

EOG Resources

Earnings on Goods, Rock!

- From COVID-19 to Saudi Arabia and Russia oil price war, the entire market experienced major sell-offs in 1Q'20. EOG experienced a -6.1% net margin for the year with a negative 2.9% return on equity.
- Moreover, the firm had huge operations cuts and cuts in investments. The production was reduced drastically and overall net loss in comparison to profits the year before.
- Moving forward, EOG has great expectations for the coming years and started showcasing growth in the year of 2021. With one of the highest FCF in the energy industry, the firm expects to grow 8% to 10% rate.
- The Company's efficient use of double premium wells has lets to greater efficiency, better returns, and lower overall costs. The Company boosted its annual dividend by 10% after its fourth-quarter adjusted profit and expects to do the same for the coming years.
- EOG is trading at an NTM EV/EBITDA multiple of 5.5x, an~8% discount to its 1-year average multiple of 6x.

Symbol	NYSE: EOG
52-Week Range	$31.22 - 77.14
YTD Performance	50.15%
Market Cap (M)	$40,896
Enterprise Value (M)	$43,778
Net Debt (M)	$65,817
Dividend Yield	3.0%
NTM P/E	14.22x
NTM EV/EBITDA	5.56x
ROE	-2.9%
ROA	-1.7%

FY (Jan)	2020A	2021E	2022E
EPS			
Q1	0.55	1.25	1.30
YoY Change		*127.3%*	*4.0%*
Q2	-0.23	1.19	1.21
YoY Change		*617.4%*	*1.7%*
Q3	0.43	1.26	1.24
YoY Change		*190.7%*	*-1.6%*
Q4	0.71	1.35	1.29
YoY Change		*90.1%*	*4.4%*
Year	1.46	4.82	5.35

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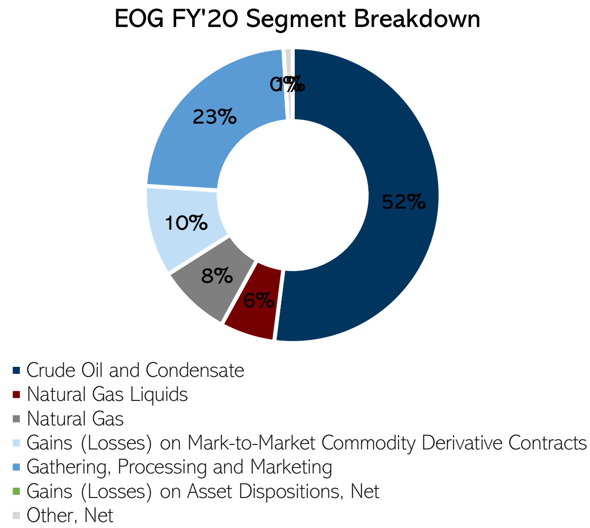
COMPANY OVERVIEW

EOG Resources Inc (EOG) is an independent upstream oil and gas Company. The Company, along with its subsidiaries, explores for, develops and produces crude oil and natural gas. The Company was formerly known as Enron Oil & Gas Company. EOG Resources, Inc. was incorporated in 1985 and is headquartered in Houston, Texas. It is one of the largest crude oil and natural gas exploration and production Companies in the United States. EOG generates revenue from the United States (97.6%), Trinidad and Tobago (1.8%), Mainland China (0.4%), and smaller markets (all <1%) such as United Kingdom, Canada, Hong Kong, Africa and Middle East, and Asia/Pacific. Its holds licenses for assets in the Eagle Ford, Bakken, Rocky Mountain, Permian Basin, Gulf Coast, Anadarko Basin, and Barnett Shale regions, among others in the US; South East Coast Consortium (SECC) block, Trindad; and Chuanzhong Block exploration in the Sichuan Basin in China. EOG reports 1Q'21 earnings in May.

BUSINESS OVERVIEW

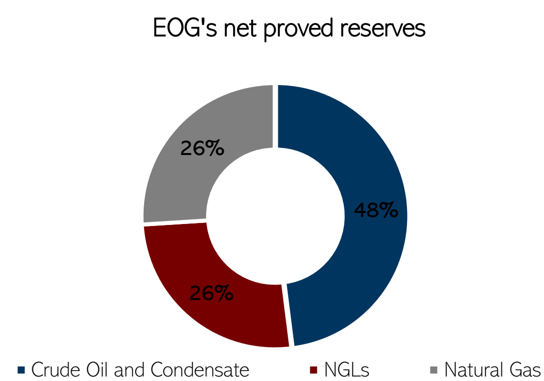
Its operations are all crude oil and natural gas exploration and production related. As of December 31, 2020, its total operating revenues were $11,032,048, of which $ 5,785,609 were crude oil and condensate, $667,514 were natural gas liquids, $837,133 were natural gas reserves, $1,144,737 were gains on mark-to-market commodity derivative contracts, $2,582,984 were gathering, processing, and marketing, $-46,883 were losses on asset dispositions, and $60,954 were from other, net. Its operations are focused on the productive basins in the United States with a focus on crude oil and, to a lesser extent, liquids-rich natural gas plays. It has operations offshore Trinidad, in the United Kingdom East Irish Sea, in the China Sichuan Basin and in Canada.



Crude Oil and Condensate (52% of FY'20 Revenue)

EOG's overall estimated net proven reserves were 3,220mm barrels of oil equivalent (MMBoe) as of December 31, 2020, with crude oil and condensate reserves accounting for 1,514mm barrels (MMBbl). On a crude oil equivalent basis, roughly 98 percent of EOG's net proven reserves were located in the United States, 1% in Trinidad, and 1% in other foreign areas at the time. Crude oil equivalent volumes are determined using a ratio of 1.0 barrel of crude oil and condensate or NGLs to 6.0 thousand cubic feet (Mcf) of natural gas.

On a crude oil equivalent basis, EOG's net proven reserves in the United States were 48 percent crude oil and condensate, 26 percent NGLs, and 26 percent natural gas as of December 31, 2020. The majority of these reserves are in well-established fields with a long history of development. EOG believes that opportunities exist to increase production through continued development in and around many of these fields and through the utilization of applicable technologies. EOG also maintains an active exploration program designed to extend fields and add new trends and resource plays to its already broad portfolio.



Total EOG crude oil volumes were 19 percent lower in the third quarter of 2019, at 377,600 barrels per day, compared to the third quarter of 2018. (Bopd). Natural gas liquids output was down 1%, and natural gas volumes were down 13%, resulting in a 14% decrease in overall Company daily production. Currently the firm is producing 420,000 barrels per day and plan to do the same for the coming years as there is oversupply of oil in the market.

CATALYSTS & DRIVERS

When there is a drill, there is some oil.

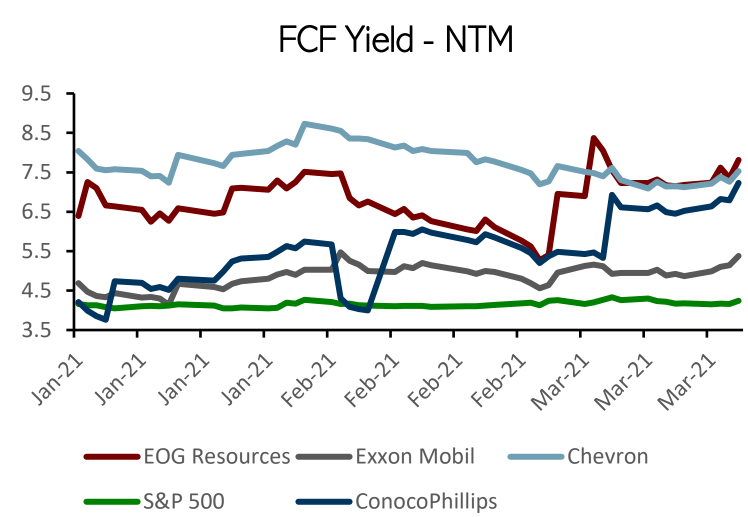
Drilling its way to success

One of the most promising and largest drivers of growth for EOG will be its investment in exploration and technology. EOG's vast inventory of premium drilling locations provides a long runway of low-cost resources. It is amongst the most technically proficient operators in the business. Initial production rates from its shale wells consistently exceed industry averages. It plans to invest $500mm from which $300mm would be invested in exploration.

The firm announced in their earnings call that it is leasing and testing across multiple plays this year. EOG believes that these areas have high potential to dramatically increase the quality of their already robust inventory. Moreover, the shift to the double premium is expected to deliver another significant step-change for the EOG's performance in the future. **They expect the efficiency of their drilling to increase and produce oil more productively at a lower cost.**

- Shift to double premium refers to wells that earn 60% direct ATROR, at $40 oil price and $2.50 natural gas price. The after-tax real rate of return (ATROR) is the actual financial value of an investment after inflation and taxes are taken into account. It's a more reliable representation of an investor's net earnings after taxes and inflation have been taken into account.
- The double premium wells are seen to be very productive for the Company. The double premium wells consumed 39% more oil than the wells they have been drilling in the last several years. These double premium wells generate higher cash flow for the firm and significantly reduced their F&G (finding and development) costs.
- During the Q4 earnings call, William Raymond Thomas, the CEO of the firm said that shifting to double-premium will make another step-change in their future performance by delivering higher returns, lower decline rates and more free cash flow potential. They have more than 10 of years of double-premium inventory and are optimistic that they will replace double-premium locations faster than they drill them.

The Company announced a major statement about its growth. Assuming markets to rebalance to pre-covid levels by year-end, EOG is positioned to developing their current drilling inventory at a moderate growth rate of 8% to 10%. This optimizes returns and free cash flow potential over time in 2022 and 2023 said by the CEO of the firm in the Q4 earnings call. Based on the forward cash flow yield graph above itself, I expect EOG to outperform its competitor firms in the industry in the coming years. The data, to form the graph above, was retrieved from FactSet, like all the other data in this document.



EOG is committed in returning cash to shareholders. Notably, the Company announced an increase of 10% dividend from the prior year dividends. Moreover, the Company added that by 2025, it is planning for zero routine flaring. By doing that, the Company aims to achieve sustainable and environmentally responsible production processes.

I believe that EOG is going to become more efficient with lower costs and higher returns as seen by the FCF and better margins and lower operating costs of the firm.

UNDERVALUATION & THESIS

EOG is trading at an NTM EV/EBITDA multiple of 5.5x, an~8% discount to its 1-year average multiple of 6x. It is currently at $74.88 and is expected to grow 8.25% to $81. Ever since February, COVID-19 has caused stock prices to plumet. Oil demand has greatly declined along with its prices, which has caused EOG and other energy Companies to take a hit. The market has started to recover from the pandemic, however, EOG still holds a lot of potential which according to me hasn't been seen yet.

- For the most part, EOG took a big hit on its earnings for the year. In the past 3 years, it was the first time the Company received negative net income, eps, EBIT margin, net margin, ROA and ROE. While Covid-19 being the major reason for the drop, EOG with other North American energy firms, struggled to operate with such low commodity prices as Russia and Saudi Arabia flood the market with foreign oil.
- In May 2020, EOG cut down on spending budget and lowered its production due to one of the worst oil pricing at the time because of the pandemic. It reduced $1bn in capital spending to $3.3bn for the year. Covid-19 induced a huge fall in demand. The firm announced shutting down of existing wells and delaying the start-up of almost 150 new wells during the same time. This was all due to the decrease in the demand because of the pandemic and now the firm plans to reopen the wells with better technology.
- EOG value didn't reduce just because of the pandemic but also due to the Trump administration in the year 2020. According to the government database, the Trump administration has cut royalties for many drilling firms extracting oil and gas on federal lands, while the industry seeks relief from low energy prices. Timothy K. Driggers, the CFO of the Company, said it had not requested royalty cuts on its federal leases, but has stakes in leases operated by other Companies that sought relief.
- In Q2 earnings report for 2020, the Company reported a net loss was $909.4mm, for the second quarter ended June 30, from a profit of $847.8mm for the year 2019. Similarly, it reported a net loss of $42mm, for the third quarter ended Sept. 30, compared to a profit of $615mm, for a year earlier.

I believe EOG was trading at a fair multiple prior to the pandemic and it now EOG's properly reflects its potential to grow revenues in FY'21 and '22. As seen with one of the highest earning FCF in the industry, the Company is expected to become better in coming years. One of the major influencers would be its focus in double premium wells and the results they develop.