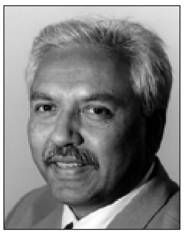
# Exxon Mobil: Wow, is it cheap for an oil stock!

*Company's reluctance to buy into the high-oil-price scenario may have sent the wrong message to investors*

**By Sunil Vidyarthi**



**Sunil Vidyarthi**

How would you like to be a guy who bought a piece of real estate 10 years ago, then decided that it was getting too richly priced and sold it just before the market took off in 2003? Well, I know of a famous economics professor who said the world was going into a depression back in 1990. He sold his Manhattan apartment to live in a rental, or so he said in his book. I hope he later bought it back.

Stories like these are all too common in the money-making business and particularly so, in the stock market. Apparently, most brokers sold their holding in TSX Group shortly after it went public, only to watch the stock more than quadruple in a couple of years.

I suppose moves like the ones in real estate and Google, where the asset goes to bubble status, are totally unpredictable and can't be helped. But how do you explain a company like **Exxon Mobil Corp.** (XOM-NYSE, $58.92, 972-444-1000, *www.exxonmobil.com*) in the energy industry?

It is no secret that all you had to do until recently is say that you have a hole in the ground with the prospect of oil, gas, or something that may look like oil some day, and your stock would be jumping through double. Valuation didn't matter, size didn't matter and even geography, which at one time kept a lid on stocks like Nexen and Talisman, didn't matter.

Recently, a Nigerian-based oil company issued new shares in the midst of killings and bloody struggle in that country with quite unexpected success. So what is eating Exxon? And would changing the suit in the corner office make the difference?

First, a little about this giant, worth about $363 billion in market capitalization with a profit, yes net income not sales of $36 billion last year. Exxon Mobil operates as a petroleum and petrochemicals company. It primarily engages in the exploration, production, and sale of crude oil and natural gas; and manufacture, transportation, and sale of petroleum products.

The company also manufactures and markets basic petrochemicals, including olefins, aromatics, polyethylene, fluids, synthetic rubber, oriented polypropylene packaging films, plasticizers, synthetic lubricant basestocks, zeolite catalysts, polypropylene plastics and various specialty products.

In addition, Exxon Mobil has interests in electric-power generation facilities. Its other products include lube basestocks and petroleum specialties, such as waxes, process oils, and asphalt. The company operates in about 200 countries worldwide, including the United States, Canada, Europe, Asia-Pacific, Africa, South America, the Middle East, and the Caspian area. Exxon Mobil was founded in 1870 and is based in Irving, Texas.

And to spray some salt on the wounds of all corporations, Exxon got it wrong how high oil prices would go. It has notoriously been expecting a collapse. And maybe, it is that view that has kept investors away from the stock, relatively speaking. Now don't get me wrong, XOM has outperformed the DOW and S&P 500 in the last five years, scoring more than 50 per cent, but its own subsidiary, Imperial Oil is up by a mere 300 per cent (both in U.S. dollar terms) in the same time period.

Normally, we blame such outliers on factors such as earnings growth and return on equity, or at least some of us fundamentally-oriented investors do. Well using my general valuation model, this stock would be considered dirt cheap as it had a revenue growth of 20 per cent and earnings increase of 27 per cent (year over year) in the last quarter. The return on equity was a whopping 34 per cent. Such numbers were the hallmark of pharma and software companies in their heyday, and then they traded at multiples of 20 and 30, not 10, as is the case for Exxon today.

So, it looks like if you tell people certain things often enough, they start to believe it, even though the facts may be completely contrary to what is being said. Exxon and several others have openly questioned the theory that there is scarcity of oil and that current prices will last.

Investors who buy this stock seem to believe that and are unwilling to pay more than 10 times earnings for the security, even though learned analysts reflect no sudden decline in earnings or cash flow next year. Or, could it be that Exxon is right and the rest of the oilpatch is taking you for a ride, including its own subsidiary, Imperial Oil? Unfortunately, we won't be able to tell until the bubble has burst.

But actions speak louder than words and Exxon is taking action, albeit less forcefully than some of its big competitors. It intends to spend over $20 billion in capital expenses to find more oil, as much as two million barrels per day, and grow some of its refining and chemicals business.

The question, of course, is, how will you do with this stock? That really depends on whether you want high returns at a higher risk or you want to double your money in the next five years as in the last five. I personally like the odds with Exxon and fret more about some of the juniors and even mid- tier Canadian companies, which have been on a roll.

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