



Independent Stock Idea

November 6, 2009

rating: buy
s&p 500: 1069

Marathon Oil (MRO) Refinery Expansion Nearly Complete

| | | | |
|------------------------------------------------------------------------------------------------------------------------------|---------|----------------------------------------------------------|-------|
| <i>Symbol</i> | MRO | <i>Ebitda Next Twelve Months ending 9/30/10 (US\$mm)</i> | 6,900 |
| <i>Rating</i> | Buy | <i>North American Natural Gas/Ebitda (%)</i> | 6 |
| <i>Price (US\$/sh)</i> | 33.68 | <i>Natural Gas and Oil Production/Ebitda (%)</i> | 75 |
| <i>Pricing Date</i> | 11/6/09 | <i>Adjusted Reserves/Production NTM</i> | 9.3 |
| <i>Shares (mm)</i> | 711 | <i>EV/Ebitda</i> | 5.2 |
| <i>Market Capitalization (US\$mm)</i> | 23,900 | <i>PV/Ebitda</i> | 7.2 |
| <i>Debt (US\$mm)</i> | 11,500 | <i>Undeveloped Reserves (%)</i> | 31 |
| <i>Enterprise Value (EV) (US\$mm)</i> | 35,500 | <i>Natural Gas and Oil Ebitda (US\$/boe)</i> | 34.40 |
| <i>Present Value (PV) (US\$mm)</i> | 49,200 | <i>Present Value Proven Reserves(US\$/boe)</i> | 22.30 |
| <i>Net Present Value (US\$/share)</i> | 53 | <i>Present Value Proven Reserves(US\$/mcf)</i> | 3.72 |
| <i>Debt/Present Value</i> | 0.23 | <i>Earnings Next Twelve Months (US\$/sh)</i> | 3.24 |
| <i>McDep Ratio - EV/PV</i> | 0.72 | <i>Price/Earnings Next Twelve Months</i> | 10 |
| <i>Dividend Yield (%/year)</i> | 2.9 | <i>Indicated Annual Dividend (US\$/sh)</i> | 0.96 |
| Note: Estimated cash flow and earnings tied to one-year futures prices for oil and natural gas. | | | |
| Reported results may vary widely from estimates. Estimated present value per share revised only infrequently. | | | |
| Estimated present value presumes a long-term price for oil of US\$75 a barrel and natural gas, \$8 a million btu. | | | |
| For historical research on Marathon since 2001 see http://www.mcdep.com/3mro.htm | | | |

Summary and Recommendation

Analyzing third quarter results released November 3, we reaffirm estimated Net Present Value (NPV) of \$53 a share for buy-recommended **Marathon Oil (MRO)**. On that basis unlevered appreciation potential is 39% to a McDep Ratio of 1.0 where stock price would equal NPV. Unlevered cash flow (Ebitda) and earnings showed nice gains from the second quarter low, though not as much as in our expectations. The new rising trend appears likely to continue in the next few quarters (see table [Next Twelve Months Operating and Financial Estimates](#)). Compared to U.S. peers, Marathon's NPV is concentrated more on downstream at 26% and less on natural gas at 13% (see table [Functional Cash Flow and Present Value](#)). The outlook for upstream production earnings appears positive with futures prices for the next six years for oil trading above the 40-week average (see chart [Six-Year Commodity Price Meter](#)). Downstream, Marathon will be completing the refinery expansion at Garyville, Louisiana before year end. After planned maintenance on the existing units, the full capacity of the expanded refinery will be available in the spring, in time for next year's gasoline season. Marathon is an efficient refiner/marketer in a competitive business sensitive to rebounding economic activity. In a more profitable stage of the refining cycle, management may again contemplate spinning off the downstream business into a new publicly traded company.

Kurt H. Wulff, CFA



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| Marathon Oil Corporation | | | | | | | | | |
|------------------------------------------------------|----------------|----------------|----------------|-----------------|---------------|----------------|----------------|----------------|-----------------------------------|
| Next Twelve Months Operating and Financial Estimates | | | | | | | | | |
| | | | | | | | | | <i>Next Twelve Months</i> |
| | <i>Q3</i> | <i>Q2</i> | <i>Q3</i> | <i>Q4E</i> | <i>Year</i> | <i>Q1E</i> | <i>Q2E</i> | <i>Q3E</i> | <i>9/30/10</i> |
| | <i>9/30/08</i> | <i>6/30/09</i> | <i>9/30/09</i> | <i>12/31/09</i> | <i>2009E</i> | <i>3/31/10</i> | <i>6/30/10</i> | <i>9/30/10</i> | <i>9/30/10</i> |
| Volume | | | | | | | | | |
| Natural Gas (mmcf) | | | | | | | | | |
| U.S. (or North America) | 426 | 365 | 339 | 339 | 367 | 339 | 339 | 339 | 339 |
| Overseas (or Int'l) | 502 | 593 | 528 | 528 | 576 | 528 | 540 | 540 | 534 |
| Total | 928 | 958 | 867 | 867 | 942 | 867 | 879 | 879 | 873 |
| Days | 92 | 91 | 92 | 92 | 365 | 90 | 91 | 92 | 365 |
| Oil (mbd) | 256 | 307 | 265 | 265 | 273 | 265 | 265 | 265 | 265 |
| Total gas & oil (bcf) | 227 | 255 | 226 | 226 | 942 | 221 | 225 | 227 | 899 |
| Total gas & oil (mbd)) | 411 | 467 | 410 | 410 | 430 | 410 | 412 | 412 | 411 |
| Price | | | | | | | | | |
| Natural gas (\$/mcf) | | | | | | | | | |
| Henry Hub (\$/mmbtu) | 10.25 | 3.50 | 3.39 | 4.28 | 4.02 | 5.20 | 5.28 | 5.54 | 5.07 |
| U.S. (or North America) | 7.70 | 3.60 | 3.63 | 4.58 | 4.09 | 5.57 | 5.65 | 5.94 | 5.43 |
| Overseas (or Int'l) | 2.92 | 1.32 | 1.29 | 2.00 | 1.75 | 2.00 | 2.00 | 2.00 | 2.00 |
| Total | 5.11 | 2.19 | 2.20 | 3.01 | 2.66 | 3.39 | 3.41 | 3.52 | 3.33 |
| Oil (\$/bbl) | | | | | | | | | |
| WTI Cushing | 117.99 | 59.52 | 68.22 | 77.22 | 61.98 | 79.30 | 81.15 | 82.28 | 79.99 |
| Worldwide | 111.59 | 55.44 | 64.00 | 72.44 | 58.12 | 74.39 | 76.13 | 77.18 | 75.04 |
| Total gas & oil (\$/mcf) | 13.52 | 6.83 | 7.68 | 8.87 | 7.12 | 9.22 | 9.38 | 9.54 | 9.25 |
| NY Harbor 3-2-1 (\$/bbl) | 11.84 | 9.49 | 9.45 | 7.96 | 9.02 | 7.03 | 10.05 | 8.53 | 8.39 |
| Revenue (\$mm) | | | | | | | | | |
| Natural Gas | | | | | | | | | |
| U.S. (or North America) | 302 | 120 | 113 | 143 | 547 | 170 | 174 | 185 | 672 |
| Overseas (or Int'l) | 135 | 71 | 63 | 97 | 367 | 95 | 98 | 99 | 390 |
| Total | 437 | 191 | 176 | 240 | 914 | 265 | 273 | 284 | 1,062 |
| Oil | 2,628 | 1,549 | 1,560 | 1,766 | 5,796 | 1,774 | 1,836 | 1,882 | 7,258 |
| Other | 20,381 | 11,618 | 12,741 | 12,741 | 46,228 | 12,741 | 12,741 | 12,741 | 50,963 |
| Total | 23,446 | 13,358 | 14,477 | 14,747 | 52,939 | 14,780 | 14,849 | 14,907 | 59,283 |
| Expense | 20,153 | 12,110 | 13,025 | 13,156 | 47,449 | 13,103 | 13,121 | 13,035 | 52,415 |
| Ebitda (\$mm) | | | | | | | | | |
| Exploration and Production | 2,162 | 827 | 1,091 | 1,244 | 3,948 | 1,264 | 1,307 | 1,343 | 5,158 |
| Other | 1,131 | 421 | 361 | 347 | 1,542 | 413 | 421 | 529 | 1,710 |
| Total Ebitda | 3,293 | 1,248 | 1,452 | 1,591 | 5,490 | 1,678 | 1,728 | 1,872 | 6,869 |
| Exploration | 109 | 64 | 55 | 100 | 281 | 100 | 100 | 100 | 400 |
| Deprec., Deplet., & Amort. | 597 | 701 | 630 | 630 | 2,626 | 630 | 630 | 630 | 2,520 |
| Other non cash | | | | | | | | | |
| Ebit | 2,587 | 483 | 767 | 861 | 2,583 | 948 | 998 | 1,142 | 3,949 |
| Interest | 100 | 100 | 100 | 100 | 400 | 100 | 100 | 100 | 400 |
| Ebt | 2,487 | 383 | 667 | 761 | 2,183 | 848 | 898 | 1,042 | 3,549 |
| Income Tax | 870 | 134 | 234 | 266 | 764 | 297 | 314 | 365 | 1,242 |
| Net Income (\$mm) | | | | | | | | | |
| Exploration and Production | 1,037 | 60 | 516 | | | | | | |
| Other | 680 | 178 | 171 | | | | | | |
| Unallocated | (101) | 11 | (253) | | | | | | |
| Total | 1,616 | 249 | 434 | 495 | 1,419 | 551 | 584 | 677 | 2,307 |
| Shares (millions) | 711 | 711 | 711 | 711 | 711 | 711 | 711 | 711 | 711 |
| Per share (\$) | 2.27 | 0.35 | 0.61 | 0.70 | 2.00 | 0.77 | 0.82 | 0.95 | 3.24 |
| Ebitda Margin (E&P) | 71% | 48% | 63% | 62% | 59% | 62% | 62% | 62% | 62% |
| Tax Rate | 35% | 35% | 35% | 35% | 35% | 35% | 35% | 35% | 35% |

Please see disclosures on the final page.

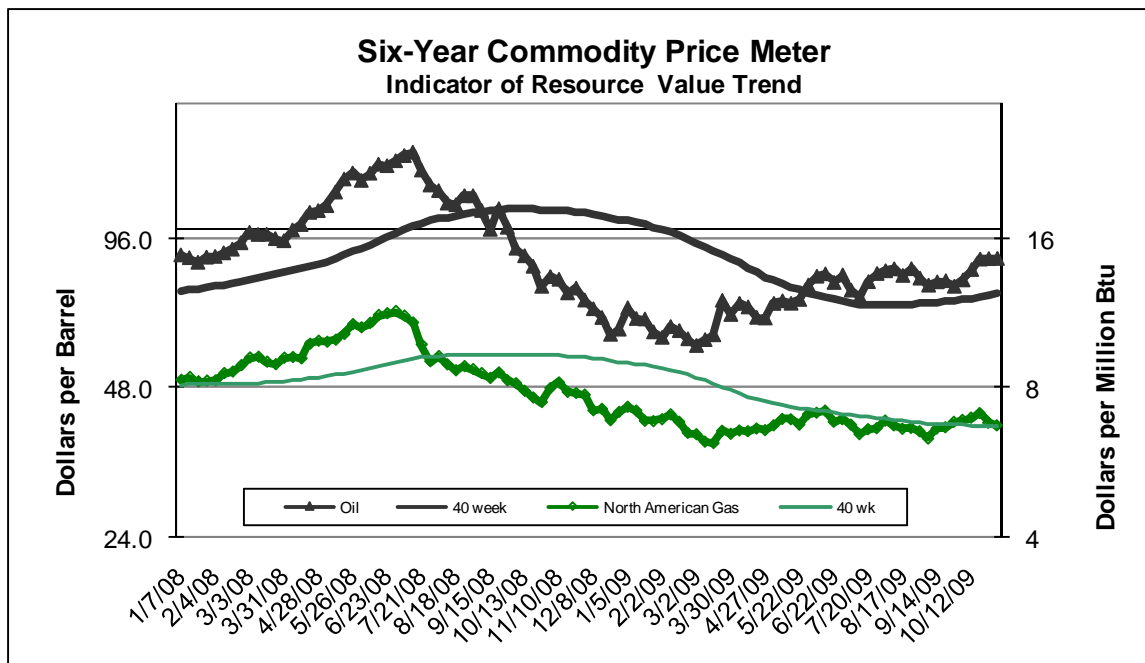
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| Marathon Oil Corporation | | | | | |
|-----------------------------------------------------------------------------|---------------|-----------------|---------------|----------------|--------|
| Functional Cash Flow and Present Value | | | | | |
| | <i>NTM</i> | <i>Adjusted</i> | <i>PV/</i> | <i>Present</i> | |
| | <i>Ebitda</i> | <i>R/P</i> | <i>Ebitda</i> | <i>Value</i> | |
| North American Natural Gas | 420 | 7.8 | 9.0 | 3,800 | 8% |
| Rest of World Natural Gas | 240 | 13.2 | 10.0 | 2,400 | 5% |
| Oil | 4,500 | 8.4 | 6.7 | 30,000 | 61% |
| Downstream | 1,710 | | 7.6 | 13,000 | 26% |
| | 6,870 | 9.3 | 7.2 | 49,200 | 100% |
| Debt | | | | | 11,500 |
| Net Present Value (\$mm) | | | | | 37,700 |
| Shares | | | | | 711 |
| Net Present Value - Standard Estimate (US\$/sh) | | | | | 53 |
| NPV Approximation by Cash Flow Multiple Depending on Reserve Life (US\$/sh) | | | | | 54 |





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