Chevron Corp.

Hess merger S-4 raises ROFR provision: CVX sees a ‘path to successful resolution’

Maintain Rating: BUY | PO: 196.00 USD | Price: 154.45 USD

27 February 2024

Equity

Doug Leggate
Research Analyst
BofAS
+1 713 247 6013
doug.leggate@bofa.com

Kalei Akamine
Research Analyst
BofAS
+1 713 247 7880
kalei.akamine@bofa.com

John H. Abbott
Research Analyst
BofAS
+1 713 247 7144
john.h.abbott@bofa.com

Carlos Escalante
Research Analyst
BofAS
carlos.escalante@bofa.com

Noah Hungness
Research Analyst
BofAS
noah.hungness@bofa.com

If the ROFR is applicable, the transaction may not close

The S-4 from CVX on the pending HES merger is the latest wrinkle (in addition to Venezuela & FTC review) with debate over right of first refusal (ROFR) provisions in the Stabroek JOA. Specific language in the S-4 states ‘if applicable to a change of control transaction and properly exercised’ the parties to JOA have a right to acquire the participating interest in the Block subject to a transaction”; but ‘only after & conditioned on the closing of such transaction.’ if the discussions among the parties do not result in an acceptable resolution and arbitration (if pursued) does not result in a confirmation that the ROFR is inapplicable to the merger, then there would be a failure of a closing condition under the merger agreement, in which case the merger may not close. If the merger agreement is terminated, HES would stay independent – and in such a case, the ROFR would not apply and resulting in an outcome where no party gains HES interest in Stabroek – unless it buys Hess itself.

CVX does not see the ROFR as applicable

The S-4 states that CVX and HES believe that the ROFR does not apply to the merger due to the structure of the merger and the language of the Stabroek ROFR provisions. Exxon (and CNOOC) believe it may – and are asserting their rights to ‘protect the value of its shareholders.’ The S-4 states that all four parties have had constructive discussions – and from our discussion with sources including CVX, those conversations are continuing. However, based on their discussions with Exxon and CNOOC and the terms of the Stabroek JOA, Chevron and Hess do not believe there is any material likelihood that the circumstances in the preceding paragraph (e.g. no confirmation that the ROFR is inapplicable) will occur.

Regardless: tax gross up makes a ROFR unattractive

As a practical point, in a scenario where the ROFR could be exercised, a tax ‘gross up’ is payable. If we assumed the $45bn value we previously attributed to 30% of Stabroek the implied incremental cost would be ~$12bn (21% US tax) for HES interest. We’re not convinced this is something XOM or CNOOC? would want to pay which leads to the most significant language in the S-4: ‘following these discussions we do not see an outcome that will ‘delay, impede or prevent consummation of the merger’. This was reinforced by our CVX discussions, stating that ‘we see a path forward to successful resolution.’

Summary: we’re not convinced ROFR is a material risk

Hess is not party to the JOA – it is Hess Exploration Guyana Limited (HEGL). Regardless all relevant parties have an obligation to examine whether its ROFR rights apply. In our view the outcome is one that introduces another layer of timing uncertainty (after the SEC, FTC). We note that Hess shares are under pressure at the time of the writing, which begs the question whether this outcome is perceived by the market as negative for Hess relative to CVX shares.

Stock Data

Price	154.45 USD
Price Objective	196.00 USD
Date Established	4-Feb-2024
Investment Opinion	B-1-7
52-Week Range	139.62 USD - 172.88 USD
Mrkt Val (mn) / Shares Out (mn)	286,013 USD / 1,851.8
Free Float	94.1%
Average Daily Value (mn)	1323.78 USD
BofA Ticker / Exchange	CVX / NYS
Bloomberg / Reuters	CVX US / CVX.N
ROE (2024E)	14.9%
Net Dbt to Eqty (Dec-2023A)	7.8%
ESGMeter™	High

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JOA – Joint Operating Agreement.

XOM holds a 45% working interest in the Stabroek block, Hess holds 30% and CNOOC 25%.

Timestamp: 27 February 2024 07:50AM EST

Price objective basis & risk

Chevron Corp. (CVX)

Our price objective of $196/sh assumes $75 Brent and $70 WTI long-term. We assume long-term HH natural gas of $4.00. We apply a long-term (post-tax) weighted average cost of capital (WACC) of 7.7%, which is based on the BofA Strategy team's assumed risk premium and a five-year monthly beta.

The risks to our price objective are: (1) commodity price volatility, (2) operational execution particularly on new projects, and (3) inability to capture the price environment due to cost pressures (opex, capex and taxation), unseen integration issues with the recently announced acquisition. Upside risks to our price objective are higher oil prices and lower cap ex spending.

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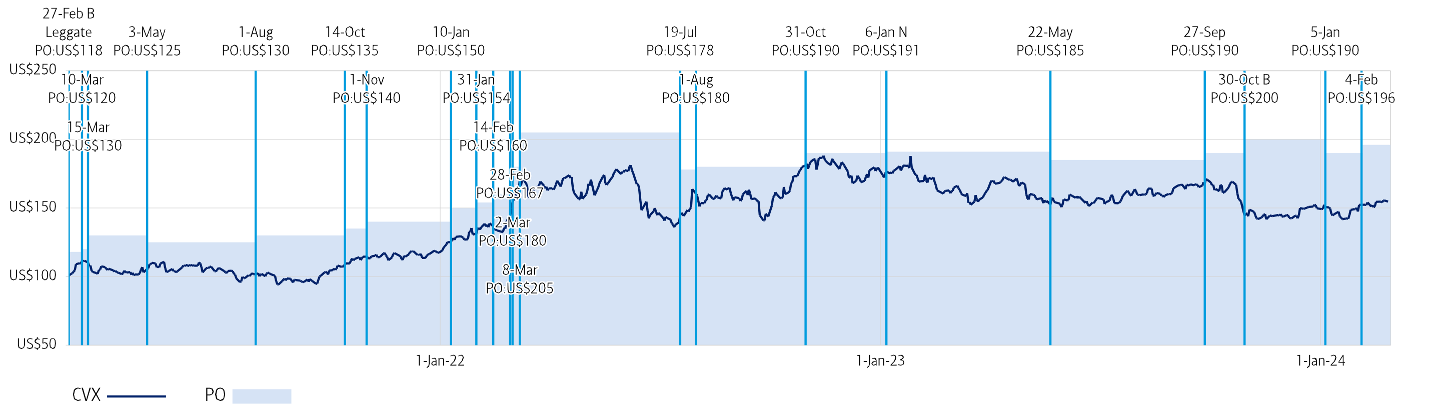
Chevron (CVX) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	83	61.48%	Buy	64	77.11%
Hold	28	20.74%	Hold	21	75.00%
Sell	24	17.78%	Sell	18	75.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

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Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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