

Stock Statistics

Ticker	CVX
Exchange	NYSE
Financial Year End	December

Market Price *	\$79.02
Market Cap *	\$158.7 bln
52-Week Hi / Low	\$56 / \$81
Average Daily Volume	> 8,000,000

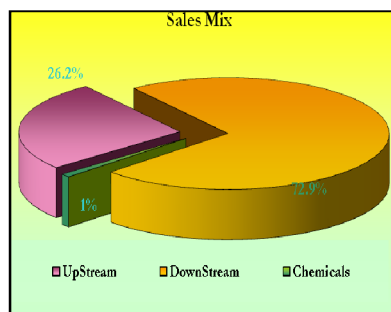


*As of previous day close

Sources: Yahoo Finance

Company Description

Chevron, a Delaware corporation headquartered in San Ramon, California, is the second-largest oil company based on market capitalization in the U.S. and the fourth-largest publicly traded oil and gas company in the world, based on proved reserves. CVX along with its subsidiaries and affiliates is operational in more than 180 countries across the globe. It operates in every aspect of the oil, gas and geothermal energy segments.



Operations are divided into three main segments: Exploration and Production (upstream); Refining, Marketing and Transportation (downstream); and Chemicals. Chevron Corporation was formerly recognized as Standard Oil of California. It merged with Gulf Oil in 1984 and was renamed Chevron Corporation. Chevron's position as an energy industry leader strengthened after the acquisition of Unocal Corporation in 2005.

Note: We are currently slightly under-weight in Energy & Materials with 10 open recommendations (out of 79 overall). That is 12.7% versus 14.3% in the S&P-500.

Investment Recommendation -- N/A -- 2011-2012 price target: \$90-\$100

Note: We initiated coverage on Chevron with a -Buy recommendation on July 1, 2010. The shares moved sharply as we were preparing this report and are up 16.6% since the recommendation 6 ahead of our benchmark (S&P-500) by 750 basis points since 7/1 (and outperforming the industry as well). I could not reiterate the recommendation here at \$79 pressing up against a two-year high. This report is now more for information purposes as opposed to an outright recommendation (given the recent move). The CVX dividend yield is 3.6%. **I would focus on the five pages in this report regarding oil price forecasts and the industry and take a closer look at CVX on a pullback to the low \$70s (if we get that).** I liked the risk-reward on this name when it traded last month in the high \$60s -- not so much here in the high \$70s, as the upside to our price target has dropped while a correction in oil prices is a concern. CVX, as opposed to most other names in the sector, is now only 20% below its 2008 high when crude prices topped \$140. Competitors XOM and COP (for example) are 30%-40% off their 2008 highs. During the last month, CVX was the best performing name in the industry and my concern is CVX and/or crude prices may be due for a correction in the near-term. Crude is + 20% since May 24. This recommendation is most suited for those looking to reduce an under-weight in the sector.

Investment Summary

- Development Pipeline** -- CVX is the second-largest U.S. oil company in terms of market capitalization and has the best oil and gas development pipeline in the industry. CVX net oil-equivalent production was 2.75M barrels per day in 2Q, 2010. Despite slowing growth, CVX is anticipated to increase production volumes by > 1% in 2011. In the longer term, the company may hit a 4% annual volume growth rate (by 2014) when some of its major Australian LNG projects are expected to hit production. Major projects for CVX include development of the (47% owned) Gorgon natural gas project in Western Australia and the deepwater in the U.S. Gulf of Mexico, offshore Western Africa and the Gulf of Thailand.
- Focus on Upstream** -- Profit margins from its downstream segment were depressed during FY09 and 1Q, 2010 due to a sharp decline in global demand for refined products reflecting the adverse impact of the economic slowdown. Q2, 2010 saw a sharp downstream margin increase. However, this may not be sustainable in the near- to medium-term as oil price have rebounded in the last two months. CVX plans to limit its refining operations to 40 markets in FY10 compared to 93 in FY09. It currently owns 1,900 filling stations, down from 3,200 in FY09. In addition, the company has shifted its focus to the natural gas segment. **According to the Energy Information Administration (EIA), the demand for natural gas is expected to grow at 1.9% per year for the non-OECD countries and at 0.6% for the OECD countries from 2007 to 2035.** CVX expects the contribution of natural gas to rise to 41% of the total volume by 2017 compared to the existing share of 31%. Over the next three years, CVX plans to begin 25 new upstream projects totaling an investment of \$1 bln.
- Cost Rationalization** -- CVX plans to slash 2,000 jobs, which includes 12% of its downstream staff and 3% of its worldwide staff in FY10, in order to realize savings in its refining segment. In FY09, CVX cut 1,900 jobs across the globe, bringing down its operating expenses by 15% (\$3.9 bln).
- Strong Financials** -- As of 30-Jun-2010, cash & cash equivalents at CVX amounted to \$9.4 bln, up from \$8.7 bln on 31-Dec-2009, reflecting the strong position of the company to cover capital expenditures of \$9.4 bln in 1H, 2010. The cash balances exceeded debt balances by \$2.7 bln at the end of 2Q, 2010
- Regulatory Concerns** -- Chevron's businesses are subject to numerous laws and regulations relating to the protection of the environment. The Deepwater Horizon oil spill in the Gulf of Mexico is expected to significantly increase political and regulatory resistance to deepwater offshore drilling. A significant portion of CVX reserve assets are in offshore deep-water. As a result of the moratorium that was implemented post-spill, Chevron abandoned its Moccasin prospect and has stopped drilling at its Buckskin site. CVX expects significant lost production in 2010 due to permit delays on the shelf and a slower ramp-up. The company has 51 lawsuits pending, the majority of which involve environmental issues. The lawsuit over oil contamination of Ecuadorian land by Texaco, owned by Chevron, is one of the long-running legal battles with \$27 billion at stake.
- International Exposure** -- International expansion of CVX businesses exposes it to various political risks. Chevron's Nigerian deepwater offshore facilities, previously assumed to be immune from terrorist attacks because of their distance from the coast, have recently become militant targets. The international upstream segment accounted for ~ 80% of the worldwide upstream investment in 2009 and ~ 70% in 2007-2008. The company garnered > 70% of its total revenue in 2Q, 2010 from its businesses outside the U.S. While the CVX significant international exposure is a risk hedge against continued lackluster U.S. demand, it also exposes the company to political uncertainties. This is particularly so, given the fact that some of the regions where it has significant asset exposure are politically volatile with unstable political constitutions. The resulting risks include embargoes, reallocation of assets, terrorism, adverse civil sentiment, etc.

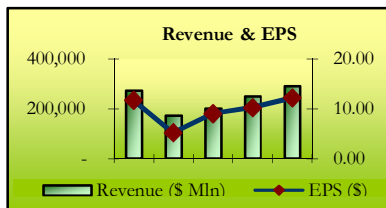
Financial Analysis

Management Guidance – CVX did not provide any revenue and earnings guidance for FY10. It projected capital expenditures to be ~ \$21.6 billion for FY10.

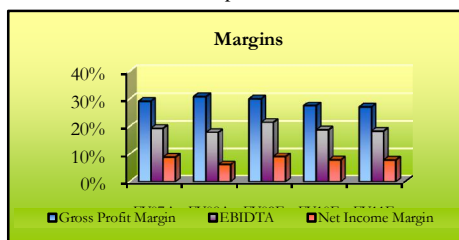
Reuters Consensus Estimates – Reuters' mean consensus estimate for 2010 revenue is \$201.9 billion and EPS is expected to be \$9.16. For FY11, the revenue estimate is \$257.9 billion and the EPS estimate is \$10.04.

Note: The estimates in this Reuters section will not always match estimates on the right side, as those are from an independent forecasting service.

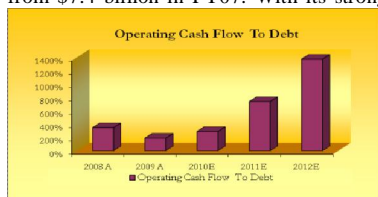
Revenue -- For 2Q10, revenue increased ~ 28% Y/Y to \$51.05B as compared to \$39.64B in 2Q09. EPS for 2Q10 was \$2.71 as compared to \$0.88 in 2Q09. Total revenues decreased ~ 37% in FY09 Y/Y to \$171.64B as compared to \$273.01B in FY08. EPS for FY09 was \$5.26 compared to \$11.74 in FY08. Revenue from the Upstream segment was \$51.3B in FY09, compared to \$82.3B in FY08. The decrease in 2009 primarily reflected lower oil and gas realizations. Revenue from the Downstream segment was \$142.9B as compared with \$219.9B in 2008. The decrease in 2009 compared to 2008 primarily reflected a decrease in prices of crude oil. Revenue from Chemicals (and other) in 2009 was \$4.5B, compared to \$6.7B in 2008.



Margins The gross margin at CVX is expected to be 27%-31% over the next three years. The company's gross margin increased to 30.8% in FY09 from 29.2% in FY08. The company witnessed an increase in EBITDA margin to 19.3% in FY08 compared to 18.6% in FY07. However, the EBITDA margin declined to 17.9% in FY09 as a result of the depressed world economy. The net income margin increased to 8.80% in FY08, as compared to 8.51% in FY07. However, the net income margin for FY09 dropped to 6.15%.



Balance Sheet & Liquidity – As of 31-Dec-09, total debt was \$10.21B which included short term debt of \$3.84B. The debt-to-capitalization ratio was 11.1% on 31-Dec-09. Cash and cash equivalents at the end of FY09 totaled \$8.7 billion. In FY08, the company's cash increased significantly to \$9.3 billion from \$7.4 billion in FY07. With its strong cash position, the company is likely to go for a share repurchase in FY11. CVX has approximately \$5.7 billion in long-term debt repayments scheduled in FY11-FY14.



Share Repurchase Program In 2007 CVX approved a share repurchase program of \$15 billion over a period of (up to) three years. The company repurchased \$8B of this approved buy-back. In the 2Q10 earnings call, CVX indicated the next round of repurchasing is likely in 4Q10 or early FY11 but not before that, despite solid cash-flows.

Dividend -- CVX has been paying quarterly dividends to its shareholders since 1997. The dividend payments at CVX have grown significantly over the years. In April 2010, CVX increased its dividend to \$0.72 cents a share.

Financial Summary

	2009A	2010E	2011E	2012E
Summary Income Statement				
Revenue	171,636	200,686	250,666	291,654
Gross Profit	52,784	60,206	68,933	78,747
EBIDTA	30,666	43,148	47,125	53,373
Interest Expense	28	74	72	38
Pre Tax Income	18,528	31,274	34,152	39,405
Net Income	10,563	18,139	19,808	22,855
EPS	5.24	9.01	10.22	12.18

Summary Balance Sheet

Cash and Equivalents	8,716	13,567	10,936	15,581
Long-term Debt	9,829	9,829	4,086	2,045
Total Debt	10,213	10,702	4,901	2,563
Net Debt	1,497	(2,865)	(6,035)	(13,018)
Shareholders' Equity	91,914	105,818	114,975	131,928
Total Asset	164,621	182,936	192,341	210,692

Summary Cash Flow

Cash from Operations	19,373	30,990	36,179	35,197
Capex	19,843	21,600	22,032	22,473
Capex, Net	18,128	19,100	19,232	19,473
Free Cash Flow	1,245	11,890	16,947	15,724
Cash Dividend	5,302	5,085	5,183	5,190

Key Ratios

Revenue Growth Y/Y	-37.1%	16.9%	24.9%	16.4%
EPS Growth Y/Y	-55.1%	72.1%	13.3%	19.2%
Gross Margin	30.8%	30.0%	27.5%	27.0%
EBIDTA Margin	17.9%	21.5%	18.8%	18.3%
Debt/EBIDTA	0.33x	0.25x	0.10x	0.05x
EBIDTA/Interest Expense	1095.21x	583.08x	636.83x	721.25x

\$ million except EPS

Significant Developments

(07/19/10) CVX in deal with KOGAS – CVX signed an agreement with KOGAS (Korea) for the delivery of 1.95 million metric tons per year of LNG from the Chevron-operated Wheatstone natural gas project in Australia.

(07/18/10) Deep Water Natural Gas Discovery in Australia -- CVX discovered two deep water Natural Gas sources in the Carnarvon Basin in the western coast of Australia -- the Clio-3 in (67%-owned) Block WA-205-P and Sappho-1 in (50%-owned) Block WA-392-P. The discovery is in line with CVX's long-term plans to build up a natural gas supply business to cater to Australia and the Asia-Pacific region.

(07/15/10) CVX in deal with Total SA -- CVX entered into a deal to sell its stake in an offshore block near Nigeria's coast-line to the French oil firm **TOT**.

(07/13/10) CVX to invest in Indonesia -- CVX announced the start of commercial production at its 110-megawatt Darajat III geothermal power plant in Garut, West Java, Indonesia. The production, operated by Chevron's subsidiary Chevron Geothermal Indonesia, Ltd., increases the total capacity at the Darajat geothermal facility to 259 MW.

(05/28/10) CVX acquired 200,000 acres of shale-gas leasehold -- CVX acquired 200,000 acres of shale-gas leasehold in Western Canada. The evaluation of these assets is expected to begin by the end of 2011.

(05/20/10) Chevron Energy Solutions in deal with Marine Corps Logistics Base -- Chevron Energy Solutions, a unit of CVX and the Marine Corps Logistics Base, announced the start of construction for the first landfill gas cogeneration project (for the Navy).

Weekly Investment Research: Chevron Corporation (CVX)

Standpoint Research 155-Variable Model / Quantitative Analysis with Fundamental & Subjective Overlay

We recently ran 150 Energy stocks through our 155-variable computer model. Refer to the *Legend* sheet in our Excel reports for the color code and description of all 155 variables used in our model. The 155-variable scoring is summarized in the 32 categories below (from roe through peg). The number in each of the cells, is the rank out of **150** stocks in the recent run. The seven cells to the right of the peg cell are coded and for internal use. For example -- a weak score for return on equity (roe) can be offset by a strong score on price-to-book (pbk). A weak score on technical indicators (**especially at the extremes**), is looked at positively if it is combined with strong scores on fundamentals and valuation. Below is the color-coded profile generated by the computer for Chevron **CVX**.

rank	ticker	roe	roa	roc	ebitda	npm	acct	eps m	rev gr	eps gr	beta	debt	stab gr
25 / 150	CVX	50	24	43	107	92	19	78	115	89	10	28	127

div I	pbk	base	rel-ma	inside	safe	pcf I	pcf II	fcf	div II	rel str	pr mo	ps	rel ps	off hi-lo
91	68	33	77	35	6	38	66	1	26	94	112	23	88	62

pred	pertix	perhis	blend	peg	deducts	t val	t fund	t prop	t misc	t tech	total score
70	73	61	15	92	4049	1363	1502	451	450	283	63.52%

The net oil-equivalent production increased by 3% to 2.75 MMBOE/d in 2Q10 compared to 2.67 MMBOE/d in the year-ago period. The increase was primarily owing to new projects started in the U.S. and Brazil along with the expansion of capacity at Tengiz in Kazakhstan. In 2Q10, the company's earnings more than tripled to \$5.41B in comparison to \$1.75B in 2Q09 as a result of higher prices for natural gas and oil coupled with improving refining margins. The upstream segment of the company contributed ~ \$4.5B of the total earnings, while the downstream segment contributed \$975M and the -Other segment revenues posted a loss of ~ 108M. The prices for refined products (such as gasoline) have a tendency to rise during second quarter owing to an influx of summer tourists in the U.S. Thus, maintaining the existing profit levels for the refineries remains a concern for the company. CVX generated ~ \$2B of cash flow in 2Q10. It declared a quarterly dividend of \$0.72 share, payable September 10, 2010, which is 10.8% higher than the dividend paid out in the year-ago period.

The full-year production guidance of CVX is 2.75 MMBOE/d, almost 2% higher than FY09 volumes, given a better overall performance of the world economy and improved sales of natural gas in Thailand. The company expects to replicate its existing performance at SGI/SGP in Kazakhstan, Frade in Brazil and Mafurneira Norte in Angola in the remaining half of FY10. Chevron's potential pipeline of development projects and remarkable recent exploration accomplishments are expected to drive the long-term success of the company. The company's latest strategy to focus on the lucrative upstream segment (primarily natural gas) both domestically and internationally should also boost EPS.

In 2Q10, CVX announced two new deepwater natural gas discoveries in the Carnarvon Basin, Clio-3 and Sappho-1. The Carnarvon Basin is located ~ 90 miles northwest of Onslow (Western Australia). These projects support the company's long-term plan to build a leading natural gas base to supply to Australia and Asia-Pacific.

Furthermore, CVX signed a Heads of Agreement (HOA) with Korea Gas Corporation (KOGAS) for the delivery of liquefied natural gas (LNG) from the Chevron-operated Wheatstone LNG project in Australia. KOGAS anticipates to procure 1.125 million tons per annum (mtpa) of LNG from Chevron as part of the same agreement. Apart from being the core customer in the Wheatstone project, KOGAS has also signed an HOA to purchase a 5% equity share in all of the Wheatstone LNG project and domestic gas processing facilities. With these developments, CVX will have an ~ 80% offtake from Wheatstone.

The company has acquired 675,000 acres in Romania and ~ 200,000 acres in Western Canada. The appraisal of the Canadian acreage is expected to begin by the end of 2011. Additionally, the company added another 1,000,000 acres in Poland. CVX along with Mitsubishi Corporation will develop the Carabobo 3 block of the Orinoco Belt in Venezuela. All three Carabobo blocks combined are anticipated to produce 1.2M barrels per day. The Carabobo blocks of Orinoco are projected to hold approximately **128 bln** barrels of oil. Chevron inked an agreement with the leading oil producer in Russia, Rosneft, to trail a deepwater prospect on the Shatsky Ridge in the Russian portion of the Black Sea.

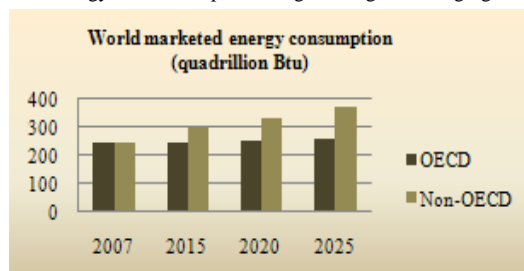
The investment decision for development of the 100% owned Duri Field (Indonesia) area 13 was sanctioned in 2Q, 2010 and this expansion project is expected to increase crude oil production by approximately 20,000 barrels per day. CVX's net oil-equivalent production in 2009 averaged 243,000 barrels per day, in Indonesia.

CVX started crude oil and natural gas production at the 37.5%-owned Peridido deepwater project located in the Gulf of Mexico. Peridido is the deepest offshore drilling and production location in the world. It is located 8,000 feet below sea level. Peridido is considered to be an impressive development in the Gulf of Mexico after the deepwater projects of Tahiti and Blind Faith. It is expected that the Peridido hub will reach its full capacity of 130,000 barrels of oil per day after the additional wells are drilled in the Great White, Silvertip and Tobago fields. The company expects its capital and exploratory expenditures to be around \$21.6B for FY10 compared to \$22.2B in the year-ago period. It plans to spend 80% of its capital and exploratory expenses on its upstream business segment. Major projects include development of Gorgon natural gas in Western Australia. It plans to liquefy and export 10M tonnes of natural gas per annum from the Greater Gorgon and Jansz gas fields. CVX holds a 47% stake in the project and is also the project operator. Other major owners in the project are Exxon Mobil (25% stake in the project), and Royal Dutch Shell (25%); Osaka Gas, Tokyo Gas and Chubu Electric Power hold the remaining 3% between them. CVX has made steady progress in its Gorgon project. The company has already signed contracts worth \$24B, and has entered into agreements for ~ 90% of the equity. The company has stated that it will not carry out any share buyback program in 3Q10 as it plans to ramp-up its capital expenditures. As a result, the company is likely to be left with surplus cash. CVX is expected to resume share buybacks in 2011. The drilling moratorium by the U.S. government, following the BP oil spill in the Gulf of Mexico has adversely impacted Chevron. The company expects a loss of ~ 10,000 barrels a day for the full year 2010 owing to the delays and a slower pace at Peridido. One of the **three** deepwater rigs of the company is presently working for the BP oil spill; the other two are waiting to resume operations.

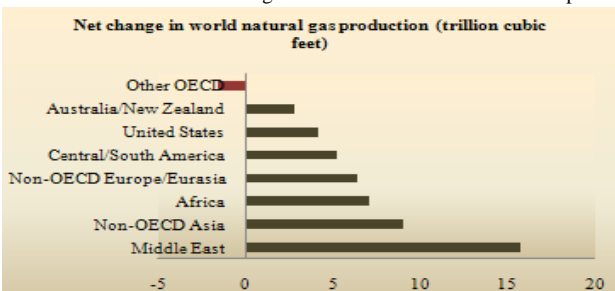
Industry Outlook

World energy demand was adversely impacted by the recession from the beginning of 2008 which continued through 2009. Demand for goods and services declined and consumption contracted 1.2% in 2008 and 2.2 % in 2009. Governments supported their economies by extraordinary fiscal and monetary stimulus which helped the world economy gain momentum in 2010. The IMF expects the world economy to grow by 3.8%. OECD economies are expected to grow by 2.0%, with the U.S. forecasted to grow by 2.5%. Japan is forecasted to grow by 1.4% and the EU by 0.9%. According to the IMF, the major contributors to the world growth is projected to be from non-OECD economies -- primarily by China at 8.8% and India at 7.7%. In 2009, oil prices increased from \$42 per barrel in January to \$74 per barrel in December. Demand for oil is expected to be sluggish in the remaining half of FY10 owing to the persisting debt crisis in the European region.

The Energy sector is expected to go through challenging times in the years to come. The positive impact of the financial stimulus provided by the various governments is expected to be temporary in nature, which will mitigate over a short-span



primarily expected to come from the non-OECD countries including India, China, the Middle East region and Latin America. Government policies related to taxes (and subsidies) are an important factor in determining the total demand of oil in the U.S. It is forecasted that demand for gasoline in the U.S. will fall on the path to recovery following the new governmental policies.



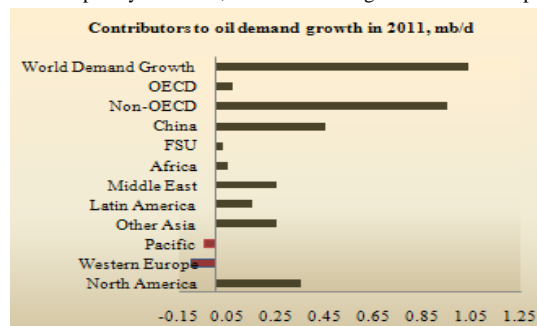
world economy. In the U.S., technologies including horizontal drilling and hydraulic fracturing have made it possible to exploit the vast shale gas resources. In Australia and the Middle East, a number of new liquefaction projects are expected to become operational which will lead to an increase in the supply of natural gas. Natural gas is traded via pipeline and can also be shipped in the form of LNG. Currently, new pipelines are under construction which will increase exports from Africa to European markets and from Eurasia to China.

BP Oil Spill

The BP oil spill in the Gulf of Mexico is the largest ever marine oil spill in the petroleum industry. This incident was caused due to the Deepwater Horizon drilling rig explosion which was triggered by a spill from the seafloor oil gusher. The spill resulted from the leakage of methane gas on 20-April-2010, which killed 11 platform workers and injured 17 others. On July 15, 2010, 95 days after the blowout, the situation was brought under control by capping the head of the well. This resulted in a loss of an estimated 4.9 million barrels of oil. According to the estimation of the quasi-official Flow Rate Technical Group, the oil well was leaking 40,000-55,000 barrels of crude oil per day. This blowout was significantly more disastrous than the 1989 Exxon Valdez oil spill, with some estimates as high as 10X-20X.

The spill is posing serious threats to the environment, has adversely impacted fishing operations and also discouraged tourism activities in the region. At its June 25, 2010 low point, BP stock had dropped 55% and had lost more than \$100 bln in market capitalization. The shares have since rebounded and recovered nearly half of that loss. BP will be subjected to certain contingent expenditures once they are proven guilty in this incident. The company has already booked \$32.2B (including \$20B for damages) as pre-tax charges related to the oil spill.

The impact of the BP oil spill will be felt globally for several years to come. However, the impact of the spill on the health of future generations, marine environment, tourism, oil and gasoline prices, and offshore drilling could only be measured as they materialize. After this incident, the oil and gas industry is expected to be subjected to greater scrutiny and calls for strict adherence to safety and environmental standards. We actually put out a recommendation on BP before the accident on March 17, 2010 and exited on July 16, 2010 at \$38.52, deciding to lock in the \$12 bounce off the June low. The shares have tracked the market -- up 6% since the July 16 downgrade. [Our six-page report on BP from Q1 can be resent on request.](#)

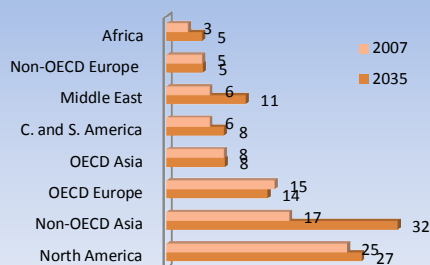


The U.S. Energy Information Administration (EIA) forecasted that oil consumption throughout the world will grow by 1.5 mmb/d in both 2010 and 2011. In 2Q, 2010 OPEC produced 29.4 mmb/d of crude oil. The EIA expects the production of oil (from the OPEC countries) to rise in order to meet demand, but not before 2011. The EIA forecasted that the Organization of Petroleum Exporting Countries (OPEC) surplus capacity should remain over 5.0 mmb/d in both 2010 and 2011 as compared to 4.3 mmb/d in 2009 and 1.5 mmb/d in 2008. The EIA forecasted that 39% of the total consumption of natural gas is expected to come from the industrial sector and 36% from the electric (generation) industry, by the end of 2035. Furthermore, the demand for natural gas is expected to rise due to the increase in production in the Middle East region and non-OECD economies coupled with an eventual recovery in the

Long Term Oil Trends

Economies around the world are expected to experience growth in the years ahead, with demand for oil accompanying them. According to the Energy Information Agency (EIA), growth will swell among non-OECD (Organization for Economic Cooperation and Development) countries, and will see GDP increasing at ~ 4.4% per year on average until 2035. For OECD countries, the outlook is less considerable, averaging growth of ~ 2% until 2035. The economic outlook for the U.S. is one of the strongest out of the OECD countries, growing at ~ 2.2% until 2018, and rising at a faster pace thereafter (see Appendix for projections from other agencies). The effect that this expansion will have on oil demand, and consequently oil prices, is anticipated to be profound. The EIA expects consumption to increase from the 86.1 million barrels per day (Mmbl/d) figure seen in 2007 to 92.1 Mmbl/d by 2020 (7% rise from 07), 103.9 Mmbl/d by 2030 (21% rise from 07), and 110.6 Mmbl/d by 2035 (28% rise from 07). Over 80% of this consumption growth will likely come from non-OECD Asia (China) and the Middle East and can be attributed to strong economic expansion in these regions.

World Liquids Consumption by Region and Country Group, Mmbl/d (2007 and 2035)



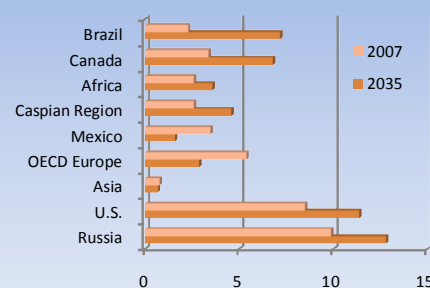
A majority of the increase in oil consumption (80%) will be the result of a surge in transportation. Emerging markets will see an escalation in personal travel and motorization over the coming years as their respective middle classes expand, and the quantity of goods shipped will continue to multiply. Consumption in OECD countries like the U.S. will grow as well, but at a much slower pace as a consequence of policy shift toward greater energy efficiency. Despite this trend, though, the U.S. will continue to expend oil at levels higher than most regions in the world. By 2035, the U.S. is anticipated to continue to be one of the largest markets for fuel consumption, using a greater number of barrels per day than China.

It has been estimated that production will increase by 25.8 Mmbl/d from 2007 to 2035, or by 1% annually over this time period. Brazil will likely see the largest increase in oil production out of the non-OPEC areas with growth of ~ 4.2% per year. The country has an immense area of sub-salt potential and has pursued petroleum legislation to promote development of the industry. The challenge that exists toward realizing this production growth is the Brazilian government. New laws have been passed requiring that Petrobras remain the sole operator and

that it maintain a minimum 30% equity holder for all of the sub-salt fields. Earlier this month legislation was put in place to tighten control over oil fields and make certain that profits are handed over to the state. While Petrobras has shown to be skilled in deepwater ventures, it may not have the resources to grow production on its own, and expanding controls will threaten foreign investment. Additionally, legislation controlling the oil fields may become more expansive as oil prices rise.

The U.S. will likely be the second largest provider of production growth over the period until 2035. Higher projected oil prices will allow for greater onshore and offshore drilling. A bulk of the increase in production will come from increased deepwater offshore fields, with most production occurring in the Pacific offshore (0.4 Mmbl/d) by 2035. Technology like horizontal drilling has encouraged domestic production, and will lead to a reversal of the trend higher of oil imports between the mid 1980s and 2005. Imports have dropped over the past few years as a percentage of fuel consumption. In 2005, 60% of fuel consumed in the U.S. was imported. As of 2009, this figure had declined to 54%. In general, over the long term, production in the U.S. is expected to increase while imports decrease.

World Liquids Production by Region and Country Group, Mmbl/d (2007 and 2035)

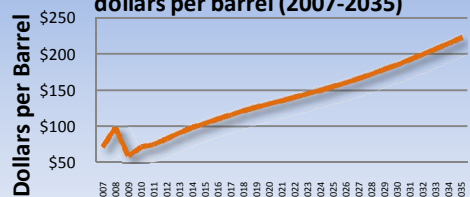


Predictions in oil prices support trends of higher production. By 2015 the price of oil is expected to reach \$95 per barrel, ascending to \$133 per barrel (in real terms) by 2035. These estimates assume that OPEC continues to maintain production at 40% of the world's supply of oil, the fraction that it has upheld in the past. These figures are dependent upon whether the organization reduces its production or non-OPEC countries contain access to production from some areas. See figure at the end of the document for historical prices and major events.

Near Term Oil Trends

Oil prices have been extremely vulnerable to expectations of demand with producers, consumers, and traders alike responding to indicators of an impending economic recovery. For example, crude futures hit one-week lows on Friday (August 6) in response to weak unemployment data. The EIA estimates that oil prices will rise to an average of \$79 per barrel over the second half of this year and rise again to \$83 per barrel by the end of 2011. The outlook rests on the idea that the world economy will slowly begin to recover generating greater demand for oil. In the near-term, world consumption is set to grow by 1.5 Mmbl/d over 2010 and again by 1.5 Mmbl/d over 2011. This growth will come from increased use in China, Saudi Arabia, and Brazil as the economic recovery in these countries outpaces that of the rest of the world. The idea that emerging non-OECD countries will contribute most to the growth in consumption supports a forecast for higher oil prices while economic indicators from the U.S. have maintained an unstable balance between both encouraging and discouraging data releases.

Projected Crude Oil Prices, nominal dollars per barrel (2007-2035)



World production is expected to increase to 86.06 Mmbl/d at the end of this year from 85.99 Mmbl/d at the end of 2Q2010 and 85.33 at the end of 2009. This figure is anticipated to be ~ 87.06 Mmbl/d in 2011. A majority of this increase in production over the next 12-24 months is likely to come from the U.S., Brazil, and Azerbaijan.

Chevron vs. Peers

Should oil prices rise as they are estimated, Chevron will be the company best strategically placed to perform well. The company has begun to invest more heavily in its Exploration and Production business, while cutting costs in its Refining business. Refining margins are greatly impacted by the cost of the process inputs, namely the cost of oil. As oil prices rise, refining margins become slimmer. So while profits from Exploration and Production may be rising with increasing oil prices, the opposite occurs in the Refining business. Thus, a greater stake in this business with a projected rise in oil prices would put a company at a disadvantage. Thankfully for shareholders of Chevron, the company has resolved to cut capital expenditures for Refining by 23%, reduce the number of filling stations it holds from 3,200 to 1,900, and trim down its Refining business to 40 markets from 92 in 2009. As of the end of 2009, refining capacity was at 2.2 Mmbl/d, far below that of peer COP. Additionally, CVX discontinued a \$15 bln share repurchase program so that it can continue investing in Exploration and Production projects. With this reinvestment, the company expects to grow production by 1% over the next 4 years and at a 4%-5% rate thereafter (as projects develop further).

Competitor, **ConocoPhillips**, has been pursuing a plan similar to that of Chevron, but with a relatively weak approach. The company has decided to sell its entire stake in LUKOIL and use the proceeds to repurchase its own shares, hardly the best investment for a company which had a decrease in production of 140,000 BOE per day as a result of normal field decline. Moreover, the company plans on reducing its refining capacity from 2.7 Mmbl/d to 2.0-2.2 Mmbl/d by 2012. These plans surfaced fairly recently, though. Only at the end of the first quarter of this year did the company articulate its plans to cut down on downstream businesses while CVX had its plan in place at the end of 2009. With regard to its E&P business, COP expects to grow production by 3% in the next two years and at a 3%-5% annual rate following 2011.

While most vertically integrated oil companies are seeking to shrink their Refining businesses going forward, Petrobras intends to grow this segment. Over the next ten years the company plans to add 1.2 Mmbl/d of refining capacity. PBR currently has a 1.9 Mmbl/d capacity, and this addition would give it a total topping 3 Mmbl/d by 2020. At this figure, Petrobras would have one of the largest Refining businesses in the world. **If oil prices rise, this strategy will have a negative impact on the company's earnings and put it at a disadvantage to peers; conversely, if oil prices decline it will give PBR a relative advantage.** Because most oil companies are seeking to reduce their Refining businesses, it is likely that they anticipate a continued rise in oil prices in the future. Petrobras' attempt to almost double refining capacity sends a message about how management feels with regard to the cost of drilling. President Inácio Lula da Silva has expressed his belief that there is little risk in offshore drilling because of the abundance of oil the country's fields are said to possess. It is with this same sentiment that the government has sought to place greater controls over the company's E&P segment, potentially deterring outside investors. Production is expected to grow by 9.7% per year over the next three years and by 7.7% each year thereafter until 2020. Though these production estimates are impressive, **it is important to note that the government seeks to use a proportion of the company's profits to fund projects for the country.** It is equally important to note the estimated increase in production compared to historical increases (~ 5.6% over the past 8 years), and whether this type of swell in production is possible. The company recently deferred an \$84.8 bln stock offering set to take place in August to fund this growth ó a move like this has the potential to upset these plans.

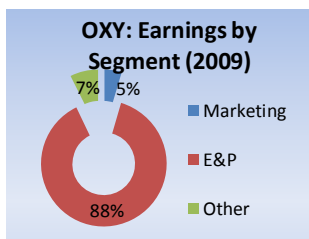
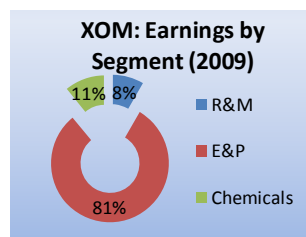
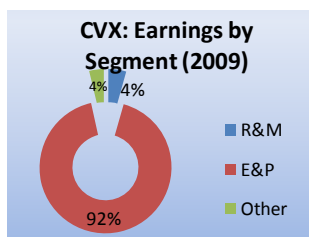
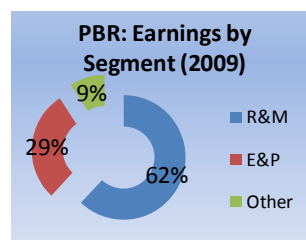
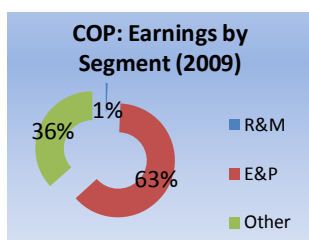
Occidental Petroleum derives its revenues solely from Exploration and Production of liquid fuels and its Chemicals business. To some this may be an advantage, because OXY does not have to exhaust resources attempting to reduce any Refining business, and has not lost earnings from the segment as a result of rising oil prices. However, while the company plans on spending more to expand E&P operations than its peers as a percentage of revenue (27.9%), this budget is less than half that which peers are planning to utilize on a straight dollar-to-dollar comparison. In the world of oil giants, the winning bid for an exploration block is often awarded to the largest competitor ó the company which can absorb such costs with the most ease. Within the next five years, OXY predicts its production will grow in the range of 5%-8%, but that would still leave OXY outside the top ten names in the industry according to market capitalization and producers.

ExxonMobil is the largest integrated oil company, with a market cap (\$317 bln) that nearly tops the # 2 and # 3 players combined [PBR at \$168 bln and CVX at \$158 bln]. XOM is the world's largest global refiner, putting it at greater risk for profit loss than its competitors in the event of higher oil prices. The company has actually worked toward increasing refining capacity in 2010 versus 2009, investing in new projects such as its Fujian expansion initiative. XOM expects to experience production growth of 2%-3% per year through 2013, a solid figure for a company of its size, but not on a relative basis (to others in the industry). XOM has done well in managing its businesses, replacing more than 100% of its production from the previous year for 16 years in a row, unfortunately for shareholders, the stock price is unchanged since 2005. It takes a lot of energy to move a company of this size and that is where the problem is.

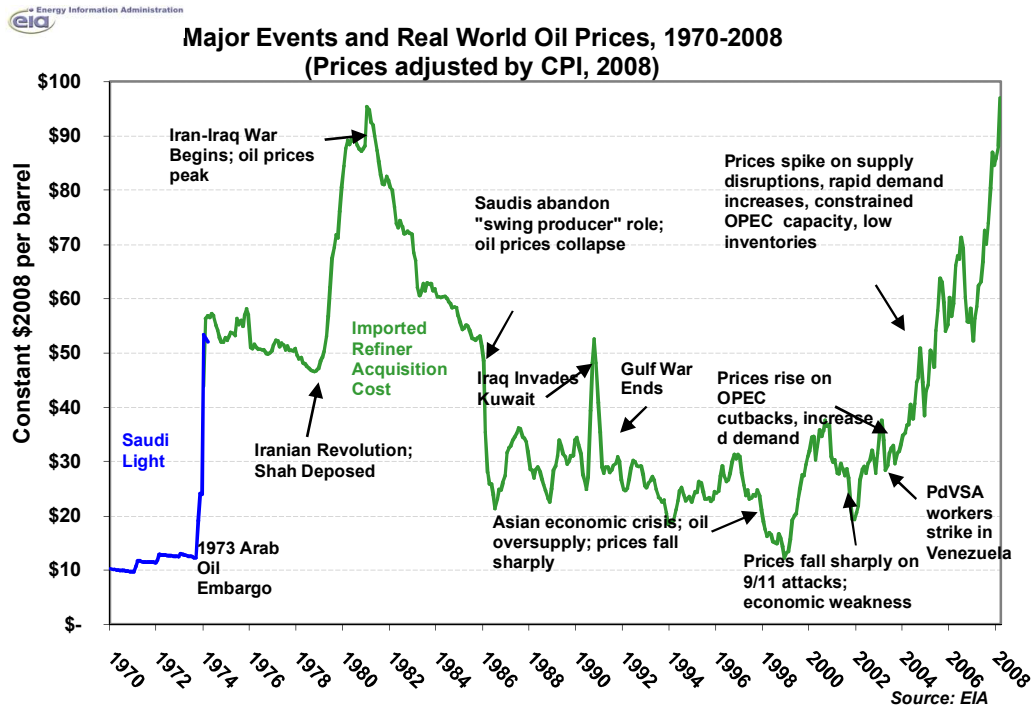
Overall, Chevron is the best prepared for a future in which oil prices are rising. It has begun implementing a strategy to reduce its holdings in the Refining segment, and has developed a plan for growing production over the mid- to long-term, eliminating its share repurchase plan and investing a greater amount of capital to do so.

	CVX	COP	PBR	OXY	XOM
Refinery Capacity (Mmbbl/d)	2.2	2.7	1.9	N/A	6.3
Number of Refineries	17	17	16	N/A	37
2010 E&P Budget as % of 2009 Revenue	13%	5.8%	19.5%	27.9%	9%

	CVX	COP	PBR	OXY	XOM
Production in Thousands of Barrel Equivalents per Day (2009)					
U.S.	484	418	4	271	311
Africa	414	78	41	N/A	685
Asia	458	132	N/A	143	286
Other	430	285	2,480	75	522
Equity Affiliates	328	442	N/A	N/A	298
Total	2,678	1,355	2,525	489	2,202



In the Paris-based International Energy Agency *World Energy Outlook* for **2008** (600-page document), that is not out-dated, the IEA gave estimates for future supply, demand, and price estimates. This outlook also included an eagerly-awaited study of 800 of the world's largest oil fields. The price of oil collapsed to < \$40 during the global recession as declines in demand and other factors pressured oil prices downwards, and topped \$140 during the bubble two years ago. As we have seen historically in financial markets, there is over-reaction to good news and bad news. Currently, we are in neither state, trading in a tight \$75-\$85 range that appears to represent fair value.



In a *Fortune* magazine article I read last year (and am quoting from here), the writer mentioned that **the IEA study makes clear that the long-term supply and demand picture for oil continues to favor higher prices.** The report estimates that energy demand will grow 1.6% per year on average through 2030, for a total increase of 45%. To meet that demand, daily oil production will need to rise from today's level of 80-85 mln barrels to (significantly) more than 100 mln barrels. The study found high and rising depletion rates at existing oil fields that will make it increasingly hard for new supplies to keep pace. So, the IEA says, **the world needs to invest some \$26 trillion through 2030 in infrastructure and exploration.**

"Given what we know, just to stay flat *in global oil production* we'd have to add the equivalent of *four Saudi Arabias* between now and 2030," said Matt Simmons, chairman of Houston energy investment bank Simmons & Co. International. Simmons is also the author of *Twilight in the Desert*, the 2005 book that argues that oil-rich Saudi Arabia's petroleum production might have peaked. "It's a very, very scary study. It's hard to argue with the data and it's ghastly what the data says." **Over the next seven years,** the IEA predicts that the price of oil will average \$100 a barrel, and rise to more than \$110 by 2030. "The era of cheap oil is over," Nobuo Tanaka, IEA executive director told reporters at a press conference in London.

In our (Standpoint Research) opinion, the IEA forecast seems reasonable, but these are volatile commodities, and I advise against taking big bets on these price movements. Traders and portfolio managers were burned in Q2, 2008 trying to pick a top at \$100, \$110, \$120 and \$130, and were again burned trying to pick a bottom in Q4, 2008 at \$60, \$50, \$40. The crude oil price seems fairly valued here in the high \$70s, but the same was said when we traded in this range three years ago – crude oil prices doubled shortly thereafter. One concern here is political as Israel runs out of patience with Iran and considers an attack on their Nuclear facilities.

As for CVX – the share price will move up and down with oil prices. We can't forecast short-term moves in oil prices. I have no crystal ball and do not know what the world news will be in the coming weeks and months. Oil prices should go to \$100 in the next few years, and so will the CVX share price. That being said, both crude oil and CVX have moved 20% in the last six weeks and may have run their course in the near-term. In the last five years, CVX is + 31% versus + 23% for crude oil. Trailing two years CVX is – 6% and crude is – 29%. Year-to-date, both are + 2%.

The table below is from our Q3 Energy sector report from July 15, 2010.
That report covered 150 stocks and can be re-sent on request.

			ROE	NET	REVENUE	EARNINGS	% OF LT	PRICE	PRICE	
	* From 07-15 sector report *	MKT	5 YR	PROFIT	5 YR HIST	5 YR HIST	DEBT :	TO	TO	DIV
N	COMPANY NAME	CAP	AVG	MARGIN	GR RATE	GR RATE	CAPITAL	BOOK	CASHFL	YIELD
1	EXXON MOBIL XOM	302995	32.0%	6.8%	1.0%	1.0%	6.0%	2.5	8.6	3.0%
2	PETROBRAS BRAZIL PBR	154819	29.5%	14.3%	31.0%	23.0%	34.0%	2.0	6.3	1.3%
3	CHEVRON CVX	146711	23.8%	7.1%	2.0%	3.0%	10.0%	1.5	5.8	3.9%
4	BRIT PETROLEUM UK BP	121876	24.4%	6.6%	-2.0%	-1.0%	19.0%	1.2	4.0	0.0%
5	TOTAL FRANCE TOT	118454	20.1%	6.4%	5.0%	1.0%	26.0%	1.5	5.1	6.0%
6	ROYAL DUTCH HOLL RDS	98995	23.5%	2.2%	-	-	20.0%	1.2	4.7	6.0%
7	ENI ITALY E	81549	24.9%	7.7%	10.0%	-1.0%	24.0%	1.2	3.7	6.6%
8	CONOCOPHILLIPS COP	78672	18.5%	4.1%	1.0%	-9.0%	29.0%	1.3	4.8	4.2%
9	STATOIL NORWAY STO	66834	26.2%	7.1%	12.0%	-7.0%	32.0%	1.9	4.4	4.4%
10	OCCIDENTAL PETR OXY	66679	26.7%	21.9%	5.0%	5.0%	8.0%	2.2	9.6	1.9%
11	SUNCOR ENE CANADA SU	49342	22.3%	6.1%	28.0%	7.0%	29.0%	1.5	11.2	1.2%
		P/S	E'PRISE	P/E	EARNINGS	EARNINGS		RV EST	RV EST	
	* From 07-15 sector report *	LATEST	VAL TO	LATEST	ESTIMATE	ESTIMATE		CUR YR	NXT YR	
N	COMPANY NAME	4 QTRS	EBITDA	4 QTRS	CURR YR	NEXT YR	CHANGE	(MILL)	(MILL)	CHANGE
1	EXXON MOBIL XOM	0.90	5.60	13.3	5.71	6.81	19.3%	389000	441000	13.4%
2	PETROBRAS BRAZIL PBR	1.33	6.17	9.3	3.62	-	N	66000	-	N
3	CHEVRON CVX	0.80	4.22	11.3	8.79	9.96	13.3%	199000	252000	26.6%
4	BRIT PETROLEUM UK BP	0.45	3.55	6.9	5.70	6.52	14.4%	293000	335000	14.3%
5	TOTAL FRANCE TOT	0.60	4.55	9.4	6.46	7.29	12.8%	149000	158000	6.0%
6	ROYAL DUTCH HOLL RDS	0.32	4.52	15.0	5.71	7.07	23.8%	347000	394000	13.5%
7	ENI ITALY E	0.69	3.29	9.0	5.05	5.95	17.8%	88000	96000	9.1%
8	CONOCOPHILLIPS COP	0.47	4.47	11.5	6.03	7.30	21.1%	192000	208000	8.3%
9	STATOIL NORWAY STO	0.82	2.00	11.6	2.16	2.59	19.9%	85000	134000	57.6%
10	OCCIDENTAL PETR OXY	3.90	8.15	17.8	5.69	7.35	29.2%	20000	24000	20.0%
11	SUNCOR ENE CANADA SU	1.87	13.27	30.4	1.55	2.64	70.3%	31000	35000	12.9%

Partial List of Sources

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End of Report

Updated Reporting Schedule –

Jul 05: S&P-500 _ # 263
 Jul 08: Individual write-up **ADBE** – original recommendation date was June 30, 2010
 Jul 11: Special Report _ # 264
 Jul 16: Energy-150 _ # 265
 Jul 20: Healthcare-200 _ # 266
 Jul 23: Individual write-up **TEO** – original recommendation date was June 14, 2010
 Jul 26: Industrials-250 _ # 267
 Jul 30: Individual write-up **GILD** – original recommendation date was July 13, 2010

Aug 03: Russell-1000 _ # 268 – 800 names with market cap > \$1 bln
 Aug 06: Russell-2000 _ # 269 – 1,140 names with market cap < \$3 bln
 Aug 10: Individual write-up **CVX** – original recommendation date was July 1, 2010
 Aug 13: Short Interest-1000 _ # 270
 Aug 17: Materials-100 _ # 271
 Aug 20: Consumer Staples-100 _ # 272
 Aug 24: Individual write-up **TBD**
 Aug 28: ADR-International-200 _ # 273

Sep 01: Individual write-up **TBD**
 Sep 04: Technology-300 _ # 274
 Sep 08: Financials-200 _ # 275
 Sep 12: Individual write-up **TBD**
 Sep 16: Short Interest _ # 276
 Sep 19: Discretionary-300 _ # 277
 Sep 24: Individual write-up **TBD**
 Sep 28: Dividends-240 _ # 278

Oct 03: S&P-500 _ # 279
 Oct 07: Individual write-up **TBD**
 Oct 10: Energy-150 _ # 280
 Oct 14: Healthcare-200 _ # 281
 Oct 20: Industrials-250 _ # 282
 Oct 24: ADR-International-200 _ # 283
 Oct 27: Special Report _ # 284
 Oct 30: Individual write-up **TBD**

*Individual write-ups to be determined and run 6-8 pages in length;
 that usually includes 2-3 pages on the respective industry
 Past reports can be re-sent on request*

*Utilities and Telecom each carry
 less than 4% weight in the S&P-500;
 sector reports for those (two) are not in our
 regular reporting rotation -- they will each be
 covered in the ADR, Russell and S&P-500 reports.*

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