

Equities

24 January 2011 | 7 pages

Halliburton Co (HAL)

Alert: Reports Strong Quarter and Maintains Improving Outlook

■ Company Update

- **Strong Quarter** – HAL reported a better-than-expected fourth quarter EPS, \$0.68 vs. \$0.60/\$0.63 our/consensus estimates. Revenues of \$5.16B were higher sequentially by 11% and exceeded \$4.77B/\$4.88B our/consensus estimates. All geographic regions saw an increase in revenues q/q. The reported results exclude a charge to discontinued operations of \$0.02/share.
- **North America Dominated** – N.A. was the primary driver of the beat (+\$0.07/share). Revenues grew sequentially by 10% to \$2,631M, which is 13% higher than our \$2,333M estimate. The strong top-line growth occurred despite the typical 4Q weather-related pressures and losses from the underutilized GOM infrastructure. HAL historically sees service intensity moderate in 4Q, but revenues grew by 10% although the rig count grew by only 4%. In the GOM, large customers remain committed to the region, but HAL does not expect a meaningful increase in activity levels in 1H11.
- **North American Margins Are the Swing Factor** – N.A. operating margins were flat at 24.0% and slightly below our 24.3% estimate. North American costs, including labor, freight, and materials, increased during the quarter. However, the company does not believe that North American margins will weaken in 2011 despite the industry's expanding pressure pumping equipment capacity, a view starkly in contrast with Schlumberger's cautious comments on Friday. Instead, HAL expects to see service prices improve in high-growth basins and believes incremental supply will be absorbed by increases in service intensity and the backlog of uncompleted wells, among other factors.
- **International Pricing Visibility Is Limited** – The company continues to cite difficulties on the pricing front, and it's unclear whether it will be able to meet the activity threshold necessary to increase pricing substantially in 2011. Mexico continues to be a drag on profitability while Iraq is ramping more quickly than expected. Mexico is in the process of repair, but no tangible evidence of a drilling resurgence in the country has surfaced, and it is unlikely to take place over the next few quarters. In Iraq, HAL has been pursuing an early-mover strategy and expects sustainable profitability by mid-2011.
- **International Results Were in Line** – International results were generally in line or slightly ahead of our operating income forecast. Results in Europe/Africa/CIS beat our estimate (+\$0.01/share), with revenues growing sequentially by 13% to \$1,066M and surpassing our \$1,023M estimate by 4% in the quarter. Operating margins of 15.7% were slightly better than our 15.0% estimate. Latin America and Middle East & Asia regions both reported operating income in line with our estimates. Latin America revenues grew sequentially by 5% to \$599M and beat our expectation of \$568M by 5%, with operating margins of 13.0% in line with our

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

estimate. Middle East & Asia revenues grew by 12% sequentially to \$864M revenues vs. our \$846M estimate, with operating margins of 19.1% slightly below our 19.5% estimate.

- **Outlook Remains Robust Long-Term** – HAL expects the typical drop-off in revenues and margins in North America and international markets in 1Q, but the company reiterated its bullish long-term view on the cycle. HAL indicated that 2011 capex is likely to be at the high end of the \$2.5-\$3.0B guidance range given during its Analyst Day presentation in November 2010. The company introduced effective tax rate guidance of 31%-33% in 2011, which is higher than the 31.1% rate in 4Q10 and in line with the 32% average in 2010.

Halliburton Co (HAL.N; US\$38.81; 1H)

Figure 1. Halliburton: Actual Results vs. Estimates and Prior Results

Halliburton (HAL) Quarterly Analysis							
	4Q'10A	4Q'10E	Difference		3Q'10A	Sequential	
Revenue	\$5,160	\$4,770	\$390	8%	\$4,665	\$495	11%
Operating Income	1,042	959	83	9%	880	162	18%
General Corporate Expenses	62	58	5	8%	62	0	0%
EBIT	980	902	78	9%	818	162	20%
Interest Expense (Income)	69	77	(8)	-10%	76	(7)	-9%
Other Expense (Income)	1	0	1	NA	7	(6)	-86%
Pretax Income	910	825	85	10%	735	175	24%
Taxes	283	276	7	2%	249	34	14%
Other	(2)	(5)	3	-60%	(1)	(1)	100%
Clean Net Income	625	544	81	15%	528	97	18%
Shares	915.0	911.0	4	0%	912.0	3	0%
EPS	\$0.68	\$0.60	\$0.09	14%	\$0.58	\$0.10	18%
Tax Rate	31.1%	33.5%	(240) bp		33.9%	(278) bp	
Margin Analysis							
Corporate Margin	1.2%	1.2%	(0) bp		1.3%	(13) bp	
EBIT Margin	19.0%	18.9%	9 bp		17.5%	146 bp	
Pretax Margin	17.6%	17.3%	34 bp		15.8%	188 bp	
Segment Analysis							
Revenue							
North America	2,631	2,333	298	13%	2,381	250	10%
Latin America	599	568	31	5%	568	31	5%
Europe/CIS/W Africa	1,066	1,023	43	4%	947	119	13%
Middle East & Asia	864	846	18	2%	769	95	12%
Operating Income							
North America	632	567	65	11%	573	59	10%
Latin America	78	74	4	6%	77	1	1%
Europe/CIS/W Africa	167	153	14	9%	139	28	20%
Middle East & Asia	165	165	0	0%	91	74	81%
Margins							
North America	24.0%	24.3%	(28) bp		24.1%	(4) bp	
Latin America	13.0%	13.0%	2 bp		13.6%	(53) bp	
Europe/CIS/W Africa	15.7%	15.0%	67 bp		14.7%	99 bp	
Middle East & Asia	19.1%	19.5%	(40) bp		11.8%	726 bp	

Source: Citi Investment Research and Analysis

Halliburton Co

Valuation

We derive our \$50 HAL price target by averaging P/E and EV/EBITDA methodologies. Our target is based on historical analysis of HAL and group multiples.

Our P/E derivation generates a price target of \$50 by applying a 17.0x multiple to our forward 12-month EPS estimate of \$2.95. The multiple is below the 23.3x peak HAL multiple reached in the most recent downturn and is well above the 6.3x trough reached at the peak of the last upturn. The multiple is based on historical analysis of HAL and relative market multiples and is within the 7.8x–33.8x historical range where the average of large cap services stocks traded over the past ten years. The median group P/E multiple was 19.9x in the most recent cycle.

Our EV/EBITDA derivation generates a price target of \$49 by applying an 8.0x EV/EBITDA multiple to our forward 12-month EBITDA of \$5.67 billion. The multiple is below the 10.9x peak HAL multiple reached in the most recent downturn and is well above the 3.7x low multiple reached at the peak of the last upturn. The multiple is based on historical analysis of HAL and relative market multiples and is within the 4.3x–14.7x historical range where the average of large cap services stocks traded over the past ten years. The median group EV/EBITDA multiple was 9.6x in the most recent cycle.

* Our forward 12-month estimate reflects the four quarters earnings stream beginning 12 months from the most recently reported quarter.

Risks

Our High Risk rating on Halliburton is based on a combination of quantitative and qualitative assessments compared with those faced by other stocks covered by Citigroup Investment Research and Analysis (CIRA). Derivation of our price target and Expected Total Return (ETR) is based on projected financial performance, which is highly dependent on the level of oil and gas exploration and production (E&P) activity. E&P activity can be significantly affected by changes in oil and gas prices. HAL's performance is particularly sensitive to the NAM natural gas and pressure-pumping markets. If the impact on the company from any of these factors proves to be greater/less than we anticipate, we believe the stock will likely have difficulty achieving our target price or could outperform it.

Appendix A-1

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Analyst: Robin Shoemaker
Covered since July 1 2008

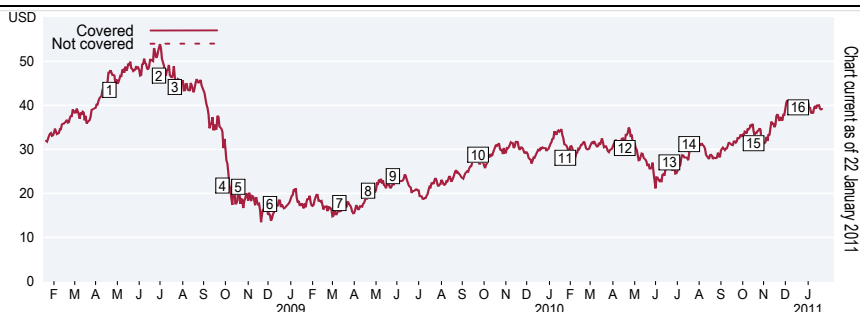


Chart current as of 22 January 2011

	Date	Rating	Target Price	Closing Price
1	21-Apr-08	1H	*60.00	47.46
2	30-Jun-08	1H	*63.00	53.07
3	22-Jul-08	1H	*64.00	46.30
4	26-Sep-08	1H	*46.00	34.00
5	20-Oct-08	1H	*36.00	20.80
6	3-Dec-08	1H	*25.00	15.10

* Indicates change

	Date	Rating	Target Price	Closing Price
7	11-Mar-09	1H	*20.00	15.77
8	21-Apr-09	1H	*23.00	19.96
9	26-May-09	1H	*27.00	22.17
10	23-Sep-09	1H	*34.00	27.35
11	25-Jan-10	1H	*40.00	31.07
12	19-Apr-10	1H	*43.00	31.57

	Date	Rating	Target Price	Closing Price
13	21-Jun-10	1H	*34.00	27.05
14	19-Jul-10	1H	*42.00	29.17
15	18-Oct-10	1H	*47.00	34.09
16	19-Dec-10	1H	*50.00	39.89

Rating/target price changes above reflect Eastern Standard Time

Halliburton Co (HAL)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Robin Shoemaker
Covered since July 1 2008

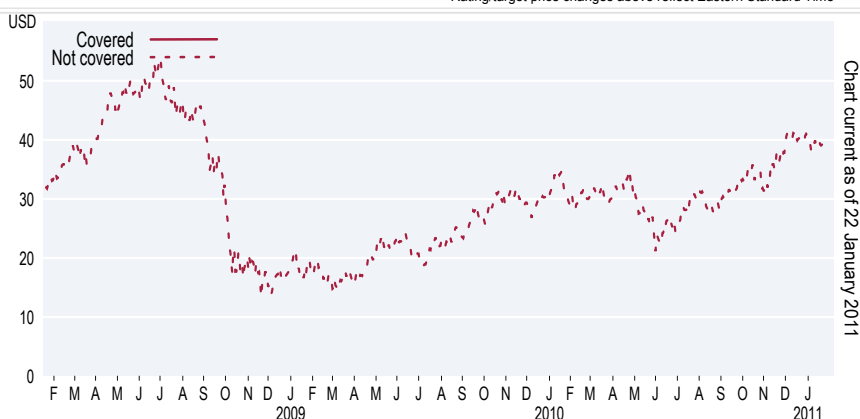


Chart current as of 22 January 2011

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