Royal Dutch Shell (RDS.B)

Updated April 30th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$72	**5 Year CAGR Estimate:**	7.9%	**Quality Percentile:**	N/A
Fair Value Price:	$55	**5 Year Growth Estimate:**	8.2%	**Momentum Percentile:**	N/A
% Fair Value:	132%	**5 Year Valuation Multiple Estimate:**	-5.5%	**Total Return Percentile:**	N/A
Dividend Yield:	5.2%	**5 Year Price Target**	$81	**Valuation Percentile:**	

Overview & Current Events

Royal Dutch Shell is an oil and gas supermajor, the second biggest behind Exxon Mobil in terms of annual production volumes. Shell is currently valued at $295 billion, again the second biggest Western oil company behind Exxon Mobil. Shell is headquartered in London (UK) as well as in Den Haag (Netherlands). There are two types of shares of the company, RDS.A shares (listed in the Netherlands) and RDS.B shares (listed in the United Kingdom).

Shell's most recent quarterly results were reported at the end of April: Shell earned $0.64 per share (non-GAAP), an increase of 39% over the prior year's quarter. This is equal to earnings of $1.28 per ADR (as one ADR is equal to two shares). Shell also managed to grow its revenues by 24% year over year during the first quarter, to $89 billion.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$10.16	$4.08	$6.56	$8.67	$8.48	$5.20	$4.72	$0.60	$1.16	$3.16	***$4.55***	***$6.75***
DPS	$3.12	$3.36	$3.36	$3.36	$3.42	$3.56	$3.72	$3.76	$3.76	$3.76	***$3.76***	***$4.40***

The earnings per share numbers in the above table don't look good at all: From 2008's levels EPS declined continuously until hitting a nadir in 2015. Since then EPS have been rising, but profits are still well below the peak levels hit around a decade ago. It would be rash to label Shell as a bad investment due to this unfortunate development, though: Oil prices hit a never-before-seen peak in 2008 (north of $140), which sent the profits of all oil explorers upwards. As oil prices headed lower since, profits normalized, which explains the 2008-2014 decline. The more recent, very steep oil price slump then wiped out almost all profits, but Shell has recovered considerably since.

When oil prices were around their lows Shell acquired BG Group (a deepwater oil and natural gas focused upstream company) in a $50 billion deal that was criticized by many at the time. Shell has, compared to other oil majors, recovered very successfully from the oil price slump. The company's production volumes are rising, its profits are growing steadily and the company produces huge free cash flows. With new projects coming online in the coming years and oil prices recovering further (during Q2 of 2018 they hit new multi-year highs) Shell has solid net earnings growth potential going forward. The company has further announced that it wants to repurchase $25 billion worth of shares in the coming years, which boosts the company's EPS growth rate further.

The company's dividend growth has not been as steady as the dividend growth history of Chevron and Exxon Mobil (as Shell has kept the dividend unchanged a couple of years in a row twice during the last decade). The company nevertheless has an excellent long term track record, as it has not cut its dividend since World War II.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	6.6	12.7	8.7	8.1	8.4	13.3	16.7	52	44	18.6	***15.8***	***12.0***
Avg. Yld.	4.7%	6.5%	5.9%	4.8%	5.1%	5.1%	4.7%	6.5%	7.4%	6.4%	***5.2%***	***5.4%***

Shell's PE ratio has moved up and down significantly over the last decade, due to the huge swings in the company's profits. Right now shares are trading at a relatively high valuation based on EPS forecasts, the median PE ratio over the last decade is in the low teens. When we focus on cash flows Shell does not look overly expensive though, shares trade at roughly 7.8 times annual operating cash flows, and at roughly 14.2 times annual free cash flows. Both of these valuation metrics are not overly high on an absolute basis, and they aren't high relative to the valuations of Shell's peers either.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	28.7%	19.5%	18.6%	22.0%	20.2%	19.6%	18.1%	12.4%	10.5%	13.4%	***15.0%***	***17.0%***
Debt/A	54.6%	52.7%	53.6%	52.8%	49.7%	49.2%	51.0%	51.8%	54.3%	51.4%	***50.0%***	***46.0%***
Int. Cov.	-	-	42.2	48.2	33.2	23.6	18.2	-	28.8	14.1	***16.0***	***20.0***
Payout	30.7%	82.4%	51.2%	38.8%	40.3%	68.5%	78.8%	627%	324%	119%	***82.6%***	***65.2%***
Std. Dev.	36.8%	32.5%	25.4%	23.3%	14.8%	13.2%	18.8%	23.3%	24.7%	13.5%	***17.0%***	***18.0%***

Shell has a huge asset base (more than $400 billion at the end of 2017), which leads to a relatively low gross profit to assets ratio. Recently that ratio has started rising again, and should continue to do so as oil prices are rising and as new assets (currently under construction but not yet producing) are coming online and start generating profits.

Shell has a high amount of liabilities ($209 billion at the end of 2017), but not all of that is long term debt for which the company has to pay interest. A big portion of those liabilities are made up by trade and other payables, retirement benefits, decommissioning and other provisions, etc. True long term debt (for which the company pays interest expenses) totals $90 billion, which is not overly high relative to cash flows or the asset base. Shell wants to lower its leverage further going forward, but the company looks financially stable already.

As one of the biggest oil and gas players with a global presence not only in the upstream segment, but also in refining, trading and the chemicals industry Shell has massive scale which makes it less dependent on individual projects and which allows for cost synergies. Shell is also continuously investing into new businesses such as wind parks.

Final Thoughts & Recommendation

Shell is highly dependent on oil prices, like all of its peers. Due to production growth, oil price tailwinds, rising cash flows and buybacks the growth outlook is relatively solid, though, and Shell offers solid total return potential. Investors can chose between RDS.A and RDS.B shares, the difference is that RDS.A shares are hit with the Dutch dividend withholding tax, whereas RDS.B shares are not hit with a withholding tax from the UK. For US based investors RDS.B shares thus look like the better choice at the moment. The Dutch government has stated that it might stop dividend taxation in the future, in that case RDS.A shares would basically be treated the same way RDS.B shares are treated now.

Total Return Breakdown by Year