Royal Dutch Shell (RDS.B)

Updated July 26th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$67	**5 Year CAGR Estimate:**	9.8%	**Volatility Percentile:**	62.8%
Fair Value Price:	$55	**5 Year Growth Estimate:**	8.2%	**Momentum Percentile:**	90.0%
% Fair Value:	122%	**5 Year Valuation Multiple Estimate:**	-4.0%	**Valuation Percentile:**	22.6%
Dividend Yield:	5.6%	**5 Year Price Target**	$81	**Total Return Percentile:**	47.0%

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 $294 billion, again the second biggest 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 in July 26. Shell earned $0.56 per share, an increase of 27% over the prior year's quarter. This is equal to earnings of $1.12 per ADR, as one ADR is equal to two shares. Shell grew its revenues by 34% year over year during the second quarter, to $97 billion. Adjusted operating cash flows totaled a massive $11.6 billion during Q2, and Shell announced the start to its $25 billion share repurchase program.

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 an inflection point 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 tremendous free cash flow. 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. During its second quarter earnings announcement Shell has stated that its $25 billion share repurchase authorization was now officially in play. This program will lower Shell's share count by ~8% over the next three years, which should boost earnings per share by close to 10%, all else equal.

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	***14.7***	***12.0***
Avg. Yld.	4.7%	6.5%	5.9%	4.8%	5.1%	5.1%	4.7%	6.5%	7.4%	6.4%	***5.6%***	***5.4%***

Disclosure: This analyst has a long position in the security discussed in this article.

Shell's valuation has moved up and down a lot over the last decade, right now shares are valued at roughly 15 times this year's earnings, which is more expensive than the historic norm. Shell's valuation will most likely decline going forward, which will be a headwind for total returns over the coming years.

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's gross profits to assets ratio has started rising again, and should continue to climb as oil prices are rising and as new projects are coming online and start generating profits.

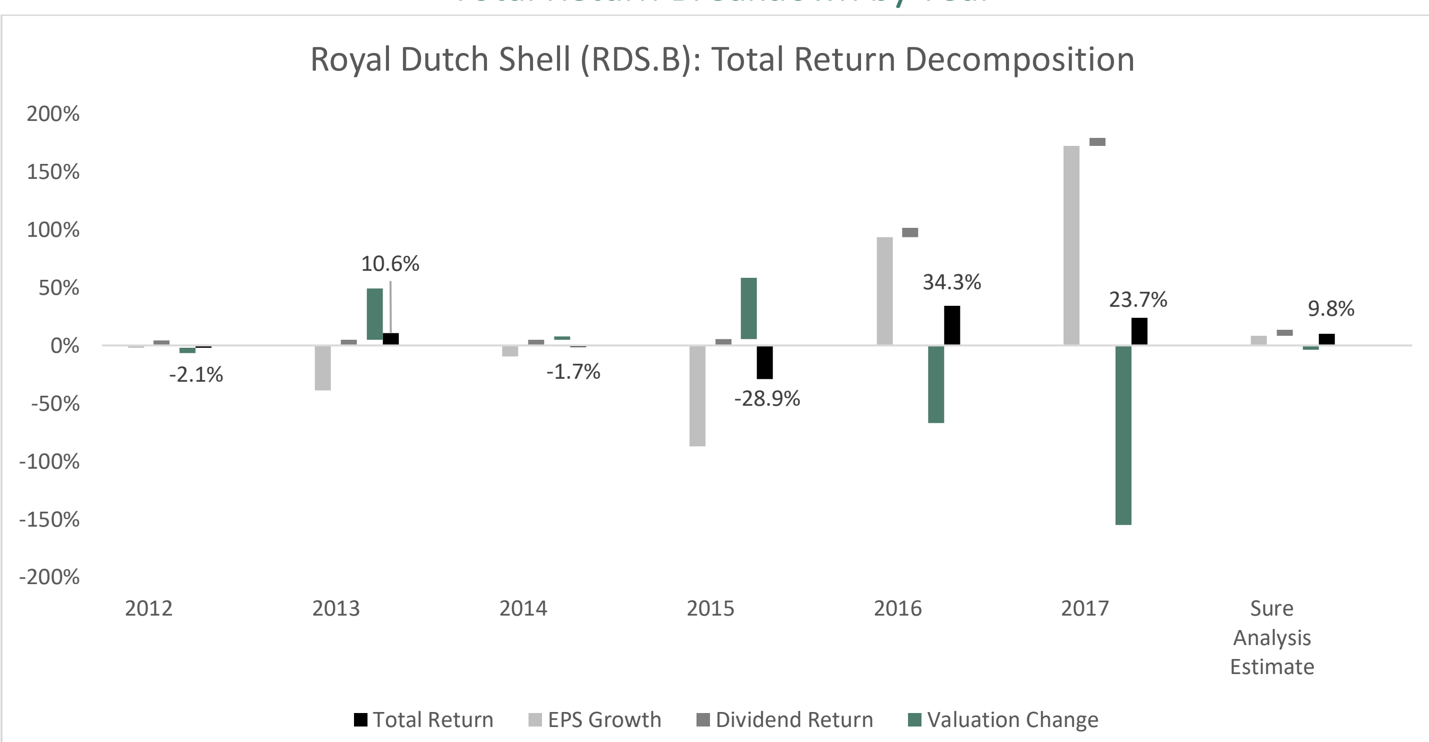
Shell has a high amount of liabilities, but not all of that is long term debt for which the company has to pay interest. True long term debt (for which the company pays interest expenses) totals $90 billion, which is not overly high relative to cash flows or the asset base. Shell wants to lower its leverage further going forward, even though 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, like its peers, highly impacted by changes in the price of oil. Recently oil prices have been on the rise, which allows for earnings and cash flow growth and rising shareholder payouts. The dividend yield from Shell is quite high and the dividend looks safe. RDS.B shares are not hit with dividend withholding taxes, whereas RDS.A shares are hit with the Dutch withholding tax. Shares should offer solid total returns in the coming years and look like a hold at current prices.

Total Return Breakdown by Year



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