



# Spark Energy Inc. (SPKE)

Updated October 10<sup>th</sup>, 2018 by Nick McCullum

## Key Metrics

<b>Current Price:</b>	\$8.46	<b>5 Year CAGR Estimate:</b>	19.9%	<b>Volatility Percentile:</b>	97.5%
<b>Fair Value Price:</b>	\$10.00	<b>5 Year Growth Estimate:</b>	8.0%	<b>Momentum Percentile:</b>	2.4%
<b>% Fair Value:</b>	84%	<b>5 Year Valuation Multiple Estimate:</b>	3.4%	<b>Growth Percentile:</b>	71.8%
<b>Dividend Yield:</b>	8.5%	<b>5 Year Price Target</b>	\$14.75	<b>Valuation Percentile:</b>	82.3%
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	96.8%

## Overview & Current Events

Spark Energy Inc. is an independent retail energy services company founded in 1999. The organization provides residential and commercial customers with alternative choices for their natural gas and electricity. Spark Energy is headquartered in Houston, Texas and currently operates in 19 states and serves 93 utility territories. The company's common stock is listed on the NASDAQ Exchange, where it trades with a market capitalization of approximately \$300 million. Spark Energy executed its initial public offering in 2014, so financial data prior to that date is unavailable for this report.

In early August, Spark Energy reported (8/2/18) financial results for the second quarter of fiscal 2018. In the quarter, revenues increased by 53.4% while operating income more than tripled and net income rose to \$23.9 million from \$4.7 million in the same period a year ago. The company's adjusted financial results were not nearly as strong. More specifically, Spark Energy reported Adjusted EBITDA of \$16.1 million, which represents a noticeable decline from the \$20.0 million of adjusted EBITDA reported in the second quarter of 2017. The decrease was primarily attributable to lower electricity unit margins as well as higher general and administrative (G&A) expenses due to a larger customer portfolio. Despite the company's strong financial performance, Spark Energy's stock price has declined by about 7% since the publication of its second quarter earnings release.

The company's main focus in the reporting period was cost-cutting. More specifically, the company stated that *"we made considerable progress in our synergy and brand consolidation efforts during the second quarter, achieving our target of annualized general and administrative cost savings of \$15 million through facility and headcount reductions. We successfully migrated a total of 110,000 customers to more cost-effective billing platforms and notified another 62,000 customers of planned platform switches that should be complete by the end of the third quarter."*

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	N/A	N/A	N/A	N/A	N/A	N/A	-\$0.01	\$0.53	\$1.11	\$1.19	<b>\$0.80</b>	<b>\$1.18</b>
<b>DPS</b>	N/A	N/A	N/A	N/A	N/A	N/A	\$0.30	\$0.73	\$0.73	\$0.73	<b>\$0.73</b>	<b>\$0.85</b>
<b>Shares</b>	N/A	N/A	N/A	N/A	N/A	N/A	6.00	6.24	33.44	34.62	<b>35.0</b>	<b>40.0</b>

Fiscal 2018 is likely to be a weak year from an earnings-per-share perspective for Spark Energy. Indeed, the company has generated a per-share loss of \$0.36 through the first six months of the fiscal year despite earning \$1.79 per share in the second quarter. Accordingly, our estimate for the company's bottom line this year is just \$0.80. Beyond next year, Spark Energy should be able to grow earnings by at least 8% per year, driven primarily by its expansion into new markets.

Important among these new markets is the company's expansion into the country of Japan. Spark Energy operates a profitable Japan business that currently has 107,000 customers acquired through a diverse set of sales channels. In the company's most recent quarterly earnings conference call, management noted that *"We continue to see development of the wholesale markets and corresponding new product alternatives over there. The business continues to outperform our business case, and we expect to begin taking distributions early next year."*

*Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.*

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	N/A	N/A	N/A	N/A	N/A	N/A	N/A	14.7	12.0	13.5	<b>10.6</b>	<b>12.5</b>
Avg. Yld.	N/A	N/A	N/A	N/A	N/A	N/A	N/A	9.3%	5.5%	4.5%	-	-

Spark Energy has consistently traded at a price-to-earnings ratio in the low double-digits since its initial public offering. Accordingly, we estimate that the firm's fair value is somewhere near a price-to-earnings ratio of 12.5. The company is trading at a price-to-earnings ratio of 10.6 today. If Spark Energy's price-to-earnings ratio expands to 12.5 over the next 5 years, this will boost the company's annualized returns by 3.4% per year during this time period.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

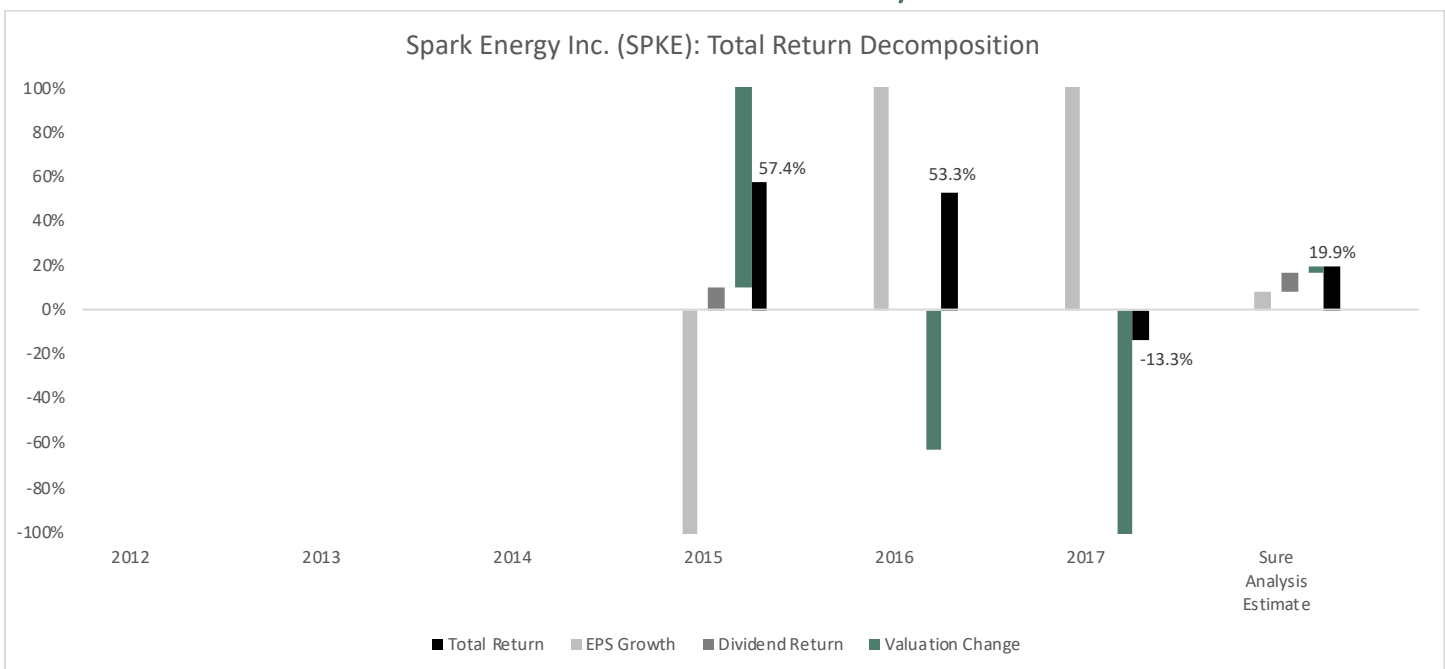
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	N/A	N/A	N/A	N/A	N/A	N/A	46.4%	72.1%	53.8%	48.6%	<b>45.0%</b>	<b>47.5%</b>
Debt/A	N/A	N/A	N/A	N/A	N/A	N/A	82.6%	79.5%	67.0%	68.1%	<b>70.0%</b>	<b>65.0%</b>
Int. Cov.	N/A	N/A	N/A	N/A	N/A	N/A	-2.7	15.5	10.8	11.5	<b>10.0</b>	<b>10.0</b>
Payout	N/A	N/A	N/A	N/A	N/A	N/A	N/A	138%	65.8%	61.3%	<b>91.3%</b>	<b>72.0%</b>
Std. Dev.	N/A	N/A	N/A	N/A	N/A	N/A	N/A	29.1%	63.7%	50.0%	<b>35.0%</b>	<b>35.0%</b>

As a small-cap energy business, Spark Energy will likely always have more volatility than its large-cap brethren. Still, the company scores surprising well on a number of our quantitative measures of business quality. More specifically, Spark Energy generates a compelling amount of gross profits from its asset base, and its interest coverage and leverage ratios are adequate. For income investors, Spark Energy earns an C rating for Dividend Safety due to its short dividend history.

## Final Thoughts & Recommendation

Spark Energy has a compelling total return profile thanks to its rapid growth rate, high dividend yield, and the potential for modest valuation expansion. We also believe that the company is suitable for risk-averse, conservative investors. Retirees should note that Spark Energy earns a C rating for Retirement Suitability, largely due to its short dividend history. With all this in mind, Spark Energy earns a buy recommendation from Sure Dividend at current prices.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	N/A	N/A	N/A	N/A	N/A	N/A	323	358	547	798
Gross Profit	N/A	N/A	N/A	N/A	N/A	N/A	64	117	202	246
Gross Margin	N/A	N/A	N/A	N/A	N/A	N/A	19.9%	32.7%	36.9%	30.8%
SG&A Expense	N/A	N/A	N/A	N/A	N/A	N/A	46	62	85	101
D&A Expense	N/A	N/A	N/A	N/A	N/A	N/A	22	25	49	43
Operating Profit	N/A	N/A	N/A	N/A	N/A	N/A	-4	30	84	102
Operating Margin	N/A	N/A	N/A	N/A	N/A	N/A	-1.2%	8.3%	15.4%	12.8%
Net Profit	N/A	N/A	N/A	N/A	N/A	N/A	0	4	14	19
Net Margin	N/A	N/A	N/A	N/A	N/A	N/A	0.0%	1.1%	2.6%	2.4%
Free Cash Flow	N/A	N/A	N/A	N/A	N/A	N/A	3	44	66	62
Income Tax Rate	N/A	N/A	N/A	N/A	N/A	N/A	-1	2	10	38

## Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	N/A	N/A	N/A	N/A	N/A	N/A	138	162	375	506
Cash & Equivalents	N/A	N/A	N/A	N/A	N/A	N/A	4	4	19	29
Accounts Receivable	N/A	N/A	N/A	N/A	N/A	N/A	65	62	112	159
Inventories	N/A	N/A	N/A	N/A	N/A	N/A	8	4	4	4
PP&E	N/A	N/A	N/A	N/A	N/A	N/A	31	33	35	41
Goodwill	N/A	N/A	N/A	N/A	N/A	N/A	4	29	101	155
Intangible Assets	N/A	N/A	N/A	N/A	N/A	N/A	114	129	251	345
Total Liabilities	N/A	N/A	N/A	N/A	N/A	N/A	39	30	52	78
Accounts Payable	N/A	N/A	N/A	N/A	N/A	N/A	33	49	78	146
Long-Term Debt	N/A	N/A	N/A	N/A	N/A	N/A	9	11	30	36
Shareholders' Equity	N/A	N/A	N/A	N/A	N/A	N/A	3.8	4.3	2.6	4.0
D/E Ratio	N/A	N/A	N/A	N/A	N/A	N/A	138	162	375	506

## Profitability Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	N/A	N/A	N/A	N/A	N/A	N/A	0.0%	2.6%	5.4%	4.3%
Return on Equity	N/A	N/A	N/A	N/A	N/A	N/A	-0.2%	38.7%	69.3%	56.6%
ROIC	N/A	N/A	N/A	N/A	N/A	N/A	-0.1%	5.6%	10.2%	7.4%

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