Royal Dutch Shell (RDS.B)

Updated November 2nd, 2018 by Jonathan Weber

Key Metrics

Current Price:	$64	**5 Year CAGR Estimate:**	10.8%	**Volatility Percentile:**	51.7%
Fair Value Price:	$54	**5 Year Growth Estimate:**	8.2%	**Momentum Percentile:**	57.7%
% Fair Value:	118%	**5 Year Valuation Multiple Estimate:**	-3.2%	**Growth Percentile:**	78.6%
Dividend Yield:	5.8%	**5 Year Price Target**	$81	**Valuation Percentile:**	23.5%
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Total Return Percentile:**	58.8%

Overview & Current Events

Royal Dutch Shell is an oil and gas supermajor, the second-largest behind Exxon Mobil in terms of annual production volumes. Shell is currently valued at $266 billion, again the second largest valuation among oil companies 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 has reported its most recent quarterly results on November 1. The company generated a very high revenue growth rate of 32.1% year over year, as its top line rose to $100.2 billion. This was primarily due to higher revenues for Shell's upstream segment, which profited from a higher oil price compared to the previous year. Shell's earnings-per-share rose to $1.36, an increase of 36% year over year. Shell has produced operating cash flows (excluding working capital changes of $2.6 billion) of $14.7 billion, which showcases Shell's ability to generate tremendous cash flows with oil prices at the current level. The company has bought back $2.5 billion worth of its own shares during Q3 and plans the same for Q4.

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***
Shares	3060	3060	3080	3110	3150	3150	3150	3200	4070	4170	***4100***	***3700***

The earnings-per-share numbers in the above table do not look good at all. From 2008's levels, earnings-per-share declined continuously until hitting an inflection point in 2015. Since then per-share profits have been rising, but are still well below the peak levels hit ten years ago. It would be harsh 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 flows. With new projects coming online in the coming years and oil prices recovering further Shell has solid net earnings growth potential going forward. The current buyback program will lower Shell's share count by ~10% over the next three years, which is a positive for investors.

The company's dividend growth has not been as steady as the dividend growth history of Chevron and Exxon Mobil. 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	***14.1***	***12.0***
Avg. Yld.	4.7%	6.5%	5.9%	4.8%	5.1%	5.1%	4.7%	6.5%	7.4%	6.4%	***5.8%***	***5.4%***

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Shell trades at 14 times this year's expected net profits, which is higher than our fair value estimate of a low-double-digit price to earnings multiple. Shell's share price will thus likely be negatively impacted by multiple contraction over the coming years. Investors get a dividend yield of 5.8% from Shell at current prices.

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%***

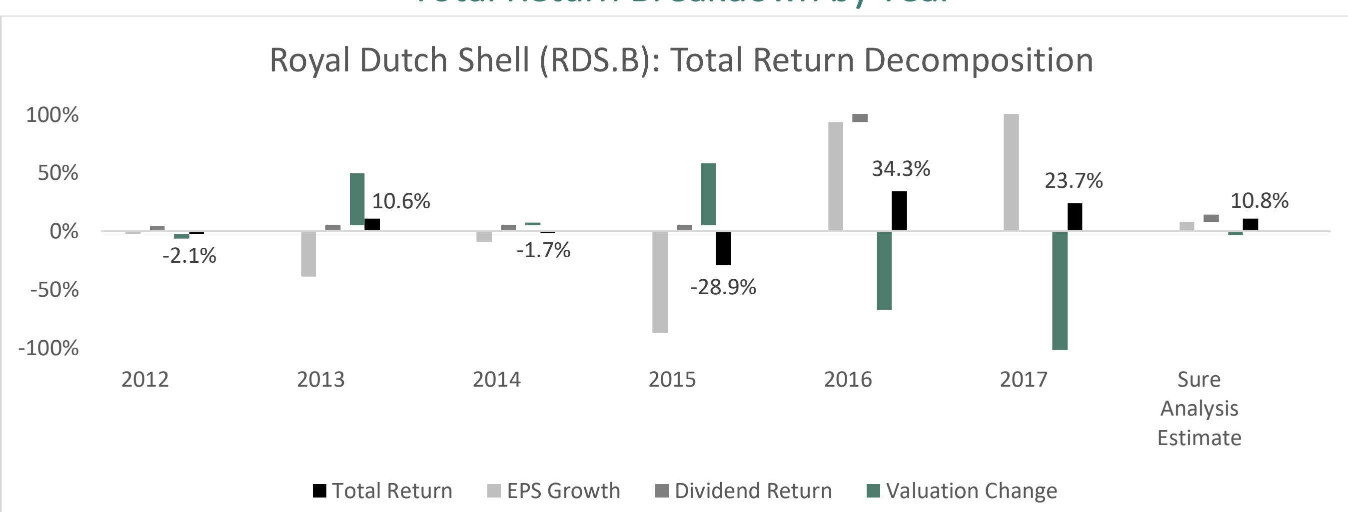
Shell's gross profits to assets ratio has started to rise again, and the ratio will in all likelihood continue to climb as oil prices are rising, and as new projects are coming online and start generating profits. Shell has a high amount of liabilities on its balance sheet, but not all of these liabilities consist of 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 Shell's cash flows or the size of Shell's vast asset base. Shell wants to lower its leverage further over the coming years, even though the company looks financially stable already.

As one of the largest 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 making investments into new, non-oil businesses, such as wind parks.

Final Thoughts & Recommendation

Shell is the second-largest publicly traded oil and gas company. It benefits from the oil price recovery to a large degree, as its earnings and cash flows show strong growth rates. The company is trading above fair value right now, but should nevertheless be able to produce compelling total returns over the coming years. Shell is, like all other oil & gas companies, dependent on commodity prices, results can thus be cyclical. The current outlook for the global oil markets is relatively positive, though. Still, Shell's valuation causes it to earn a hold 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 ($B)	465.81	285.13	368.06	470.17	467.15	451.24	421.11	264.96	233.59	305.18
Gross Profit	80655	56753	44827	60346	56598	48141	39290	15507	17590	28857
Gross Margin	17.3%	19.9%	12.2%	12.8%	12.1%	10.7%	9.3%	5.9%	7.5%	9.5%
SG&A Exp.	16906	17430	15528	14359	14465	14675	13965	11956	12101	10509
D&A Exp.	13656	14458	15595	13228	14615	21509	24499	26714	24993	N/A
Operating Profit	46868	21562	26244	42598	37722	26870	19879	-3261	2367	15481
Op. Margin	10.1%	7.6%	7.1%	9.1%	8.1%	6.0%	4.7%	-1.2%	1.0%	5.1%
Net Profit	26277	12518	20127	30826	26712	16371	14874	1939	4575	12977
Net Margin	5.6%	4.4%	5.5%	6.6%	5.7%	3.6%	3.5%	0.7%	2.0%	4.3%
Free Cash Flow	8853	-5028	410	10470	13564	465	13368	3679	-1501	N/A
Income Tax	24344	8302	14870	24450	23552	17066	13584	-153	829	4695

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets ($B)	282.40	292.18	322.56	337.47	350.29	357.51	353.12	340.16	411.28	N/A
Cash & Equivalents	15188	9719	13444	11292	18550	9696	21607	31752	19130	N/A
Acc. Receivable	82040	59328	N/A	79509	40210	39094	28393	20607	25766	N/A
Inventories	19342	27410	29348	28976	30781	30009	19701	15822	21775	N/A
Goodwill & Int.	5021	5356	5039	4521	4470	4394	7076	6283	23967	N/A
Total Liab. ($B)	153.54	154.05	172.78	177.51	174.11	176.36	180.33	176.04	222.76	N/A
Accounts Payable	85091	67161	76550	81846	42448	41927	32131	23795	28069	N/A
Long-Term Debt	23269	35033	44332	37175	33560	39417	38838	52194	77617	N/A
Total Equity ($B)	127.29	136.43	148.01	158.48	174.75	180.05	171.97	162.88	186.65	N/A
D/E Ratio	0.18	0.26	0.30	0.23	0.19	0.22	0.23	0.32	0.42	N/A

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	9.5%	4.4%	6.5%	9.3%	7.8%	4.6%	4.2%	0.6%	1.2%	N/A
Return on Equity	20.9%	9.5%	14.2%	20.1%	16.0%	9.2%	8.5%	1.2%	2.6%	N/A
ROIC	17.7%	7.7%	11.0%	15.8%	13.1%	7.6%	6.9%	0.9%	1.9%	N/A
Shares Out.	3060	3060	3080	3110	3150	3150	3150	3200	4070	4170
Revenue/Share	151	93.04	119.90	151.14	149.06	143.40	133.44	82.88	57.15	73.16
FCF/Share	2.87	-1.64	0.13	3.37	4.33	0.15	4.24	1.15	-0.37	N/A

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.