



Spark Energy Inc. (SPKE)

Updated November 28th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	\$8.88	5 Year CAGR Estimate:	15.6%	Volatility Percentile:	97.8%
Fair Value Price:	\$10.00	5 Year Growth Estimate:	5.0%	Momentum Percentile:	8.7%
% Fair Value:	89%	5 Year Valuation Multiple Estimate:	2.4%	Growth Percentile:	31.1%
Dividend Yield:	8.2%	5 Year Price Target	\$12.75	Valuation Percentile:	69.7%
Dividend Risk Score:	F	Retirement Suitability Score:	C	Total Return Percentile:	87.0%

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 94 utility territories. Spark Energy has a market cap of \$300 million and executed its initial public offering in 2014.

In early November, Spark Energy reported (11/1/18) financial results for the third quarter of fiscal 2018. In the quarter, revenues increased by 20% but adjusted EBITDA fell 5%, from \$19.6 million in last year's quarter to \$18.6 million due to a lower retail gross margin. However, net income increased from \$12.9 million to \$18.8 million thanks to non-cash gains in the hedging derivatives of the company. While these are non-cash gains, they are correctly included in earnings, as they essentially compensate the company for losses in its natural gas transactions.

While management did not provide specific guidance for next year, it stated that it expected to exceed its previous goal for cost reduction. It also expects improved performance in 2019 thanks to a better customer mix.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	N/A	N/A	N/A	N/A	N/A	N/A	-\$0.01	\$0.53	\$1.11	\$1.19	\$0.80	\$1.02
DPS	N/A	N/A	N/A	N/A	N/A	N/A	\$0.30	\$0.73	\$0.73	\$0.73	\$0.73	\$0.85
Shares	N/A	N/A	N/A	N/A	N/A	N/A	6.00	6.24	33.44	34.62	35.0	40.0

Fiscal 2018 is likely to be a weak year from an earnings-per-share perspective for Spark Energy. Indeed, the company has generated a marginal profit per share of \$0.03 through the first nine months of the fiscal year. Given the performance of the company in last year's fourth quarter and its current momentum, we expect it to earn approximately \$0.80 per share this year. It is also worth noting that Spark Energy offers very little information in its earnings reports and is hardly followed by analysts. We prefer to be conservative and assume 5% earnings-per-share growth over the next five years.

The company's expansion into the country of Japan is likely to be an important growth driver in the upcoming years. Spark Energy operates a profitable Japan business that currently has 107,000 customers acquired through a diverse set of sales channels. In the previous 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."*

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	11.1	12.5
Avg. Yld.	N/A	N/A	N/A	N/A	N/A	N/A	N/A	9.3%	5.5%	4.5%	8.2%	6.7%

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 stock is



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trading at a price-to-earnings ratio of 11.1 today. If Spark Energy's price-to-earnings ratio expands to 12.5 over the next 5 years, the stock will enjoy a 2.4% annualized boost in its returns during this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
Payout	N/A	N/A	N/A	N/A	N/A	N/A	N/A	138%	65.8%	61.3%	91.3%	83.3%

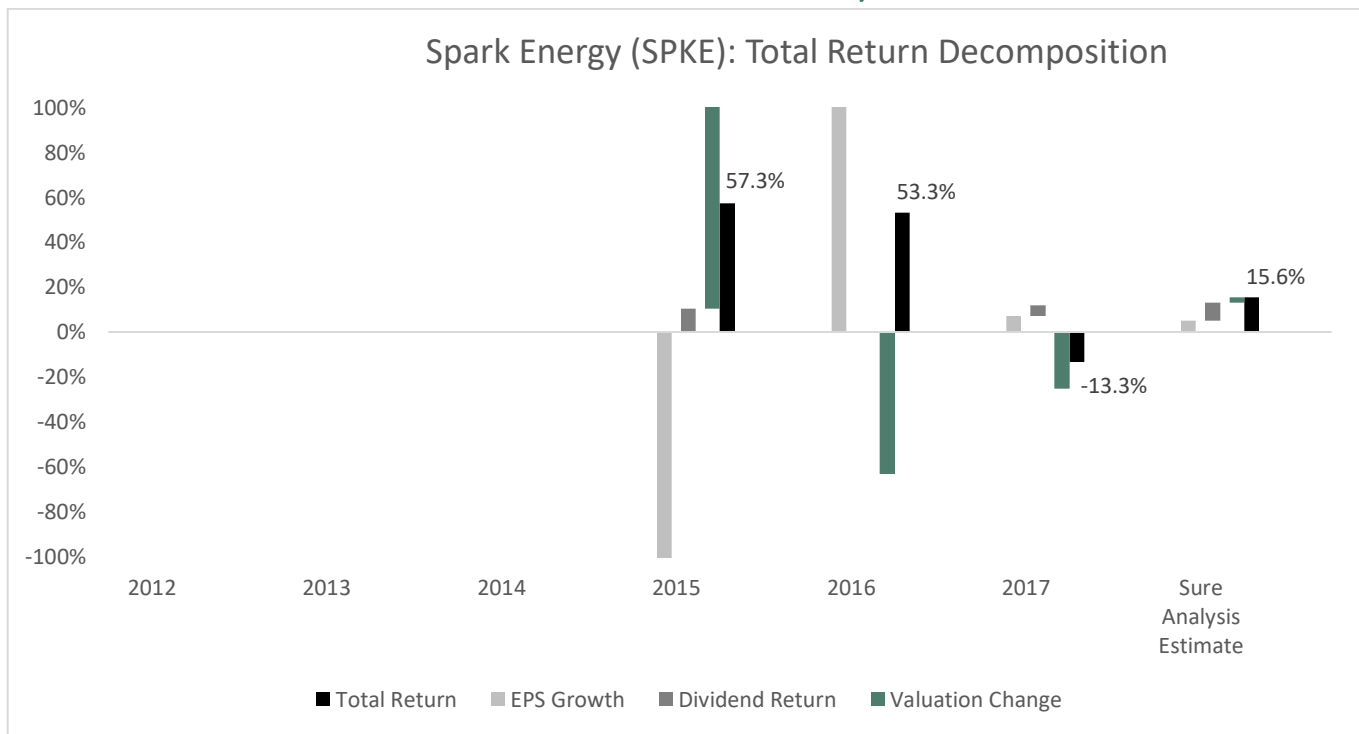
As a small-cap energy business, Spark Energy tends to be more volatile than most large cap stocks. Since the stock peaked one and a half year ago, it has lost 62%. In addition, it is hardly followed by analysts and provides little information in its reports. Therefore, this stock is suitable only for investors who have strong confidence in its business performance and can stomach dramatic swings in its stock price without panicking.

Final Thoughts & Recommendation

In our previous research report, we recommended buying Spark Energy thanks to its rapid growth rate, its high dividend yield and the potential for modest valuation expansion. Since then, the stock has advanced 5% whereas S&P has lost 3%. While the future return potential of Spark Energy has somewhat decreased, the stock can still offer a double-digit average annual return over the next five years, assisted by its 8.2% dividend yield.

As a result, it maintains its buy rating. Nevertheless, retirees should note that Spark Energy earns a C rating for Retirement Suitability, largely due to its short dividend history. Moreover, the stock is highly volatile and speculative and hence it is suitable only for investors who have strong confidence in its business model and can stomach wild swings in its stock price.

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	317	323	358	547	798
Gross Profit	N/A	N/A	N/A	N/A	N/A	84	64	117	202	246
Gross Margin	N/A	N/A	N/A	N/A	N/A	26.5%	19.9%	32.7%	36.9%	30.8%
SG&A Exp.	N/A	N/A	N/A	N/A	N/A	35	46	62	85	101
D&A Exp.	N/A	N/A	N/A	N/A	N/A	16	22	25	49	43
Operating Profit	N/A	N/A	N/A	N/A	N/A	33	-4	30	84	102
Operating Margin	N/A	N/A	N/A	N/A	N/A	10.4%	-1.2%	8.3%	15.4%	12.8%
Net Profit	N/A	N/A	N/A	N/A	N/A	31	0	4	14	19
Net Margin	N/A	N/A	N/A	N/A	N/A	9.9%	0.0%	1.1%	2.6%	2.4%
Free Cash Flow	N/A	N/A	N/A	N/A	N/A	43	3	44	66	62
Income Tax	N/A	N/A	N/A	N/A	N/A	0	-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	109	138	162	375	506
Cash & Equivalents	N/A	N/A	N/A	N/A	N/A	11	4	4	19	29
Accounts Receivable	N/A	N/A	N/A	N/A	N/A	63	65	62	112	159
Inventories	N/A	N/A	N/A	N/A	N/A	4	8	4	4	4
Goodwill & Int. Ass.	N/A	N/A	N/A	N/A	N/A	0	4	29	101	155
Total Liabilities	N/A	N/A	N/A	N/A	N/A	73	114	129	251	345
Accounts Payable	N/A	N/A	N/A	N/A	N/A	37	39	30	52	78
Long-Term Debt	N/A	N/A	N/A	N/A	N/A	28	33	49	78	146
Shareholder's Equity	N/A	N/A	N/A	N/A	N/A	36	9	11	30	36
D/E Ratio	N/A	N/A	N/A	N/A	N/A	0.77	3.81	4.30	2.58	4.02

Profitability & Per Share 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	26.4%	0.0%	2.6%	5.4%	4.3%
Return on Equity	N/A	N/A	N/A	N/A	N/A	64.6%	-0.2%	38.7%	69.3%	56.6%
ROIC	N/A	N/A	N/A	N/A	N/A	46.6%	-0.1%	5.6%	10.2%	7.4%
Shares Out.	N/A	N/A	N/A	N/A	N/A	N/A	6.00	6.24	33.44	34.62
Revenue/Share	N/A	N/A	N/A	N/A	N/A	18.93	53.81	53.82	43.08	59.80
FCF/Share	N/A	N/A	N/A	N/A	N/A	2.57	0.47	6.64	5.16	4.66

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

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