



# National Fuel Gas Co. (NFG)

Updated February 1<sup>st</sup>, 2019 by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$57	<b>5 Year CAGR Estimate:</b>	7.3%	<b>Volatility Percentile:</b>	16.8%
<b>Fair Value Price:</b>	\$64	<b>5 Year Growth Estimate:</b>	2.0%	<b>Momentum Percentile:</b>	77.1%
<b>% Fair Value:</b>	89%	<b>5 Year Valuation Multiple Estimate:</b>	2.3%	<b>Growth Percentile:</b>	5.1%
<b>Dividend Yield:</b>	3.0%	<b>5 Year Price Target</b>	\$71	<b>Valuation Percentile:</b>	62.9%
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	27.4%

## Overview & Current Events

National Fuel Gas Co. is a diversified energy company that operates in five business segments: Exploration & Production, Pipeline & Storage, Gathering, Utility, and Energy Marketing. The company's largest segment is Exploration & Production. National Fuel Gas was founded in 1902 and has grown to a market capitalization of \$4.9 billion. With 48 years of consecutive dividend increases, National Fuel Gas qualifies to be a Dividend Champion.

In late January, National Fuel Gas reported (1/31/19) its financial results for the first quarter of fiscal 2019. In the quarter, the company grew its adjusted earnings-per-share by 10%, from \$1.02 to \$1.12. Its upstream segment, which generates approximately half of the total earnings of the company, grew its production by 23% over last year but was adversely affected by the decrease of the average realized price of natural gas (after the effect of hedging), from \$2.72 to \$2.61 per Mcf. The growth in the bottom line of the company also resulted from an increase in throughput from Seneca's Appalachian natural gas production and higher earnings in the utility segment thanks to increased consumption and cold weather.

Thanks to improved outlook for the price of natural gas, management raised its earnings-per-share guidance for fiscal 2019 from \$3.35-\$3.65 to \$3.45-\$3.65. Moreover, it reiterated its guidance for 24% production growth, from 178.1 Bcfe in fiscal 2018 to about 220 Bcfe in fiscal 2019.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$2.60	\$2.65	\$3.09	\$2.63	\$3.14	\$3.52	-\$4.50	-\$3.43	\$3.30	\$3.34	<b>\$3.55</b>	<b>\$3.92</b>
<b>DPS</b>	\$1.32	\$1.36	\$1.40	\$1.44	\$1.48	\$1.52	\$1.56	\$1.60	\$1.64	\$1.68	<b>\$1.72</b>	<b>\$1.92</b>
<b>Shares</b>	80.5	82.1	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0	<b>\$87.0</b>	<b>90.0</b>

National Fuel Gas' earnings have barely grown over the last ten years. Earnings-per-share have compounded at a rate of 0.5% per year over the last 10 years. With that said, this includes a difficult ten-year stretch that includes both the 2007-2009 financial crisis as well as the precipitous drop in natural gas prices that began in 2014. We are forecasting 2% long-term earnings-per-share growth for this Dividend Champion, which allows us to calculate a 2024 earnings-per-share estimate of \$3.92. Moreover, we have raised our forecast for the earnings-per-share of this year by 3%, from \$3.45 to \$3.55, thanks to improved outlook for the price of natural gas.

Investors should note that 90% of the production of National Fuel Gas is natural gas. Therefore, as the Exploration & Production segment generates about half of total earnings, the earnings of the company greatly depend on the price of natural gas. As a result, there is always great uncertainty in the long-term forecasts of the earnings of this company.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	15.5	13.4	18.5	21.4	19.3	18.6	20.6	---	---	17.2	<b>16.1</b>	<b>18.0</b>
<b>Avg. Yld.</b>	2.6%	3.8%	2.8%	2.1%	2.8%	2.5%	2.1%	2.5%	3.1%	2.9%	<b>3.0%</b>	<b>2.7%</b>

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National Fuel Gas is trading at a price-to-earnings ratio of 16.1. For context, National Fuel Gas has traded at a price-to-earnings ratio of 18.1 over the last decade. We believe an earnings multiple around 18 represents an approximation of fair value for this blue-chip Dividend Champion. If the company returns to fair value over the next five years, annualized returns will receive a 2.3 percentage point boost.

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

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	50.8%	51.3%	45.3%	54.8%	47.1%	43.2%	N/A	N/A	49.7%	50.3%	48.5%	49.0%

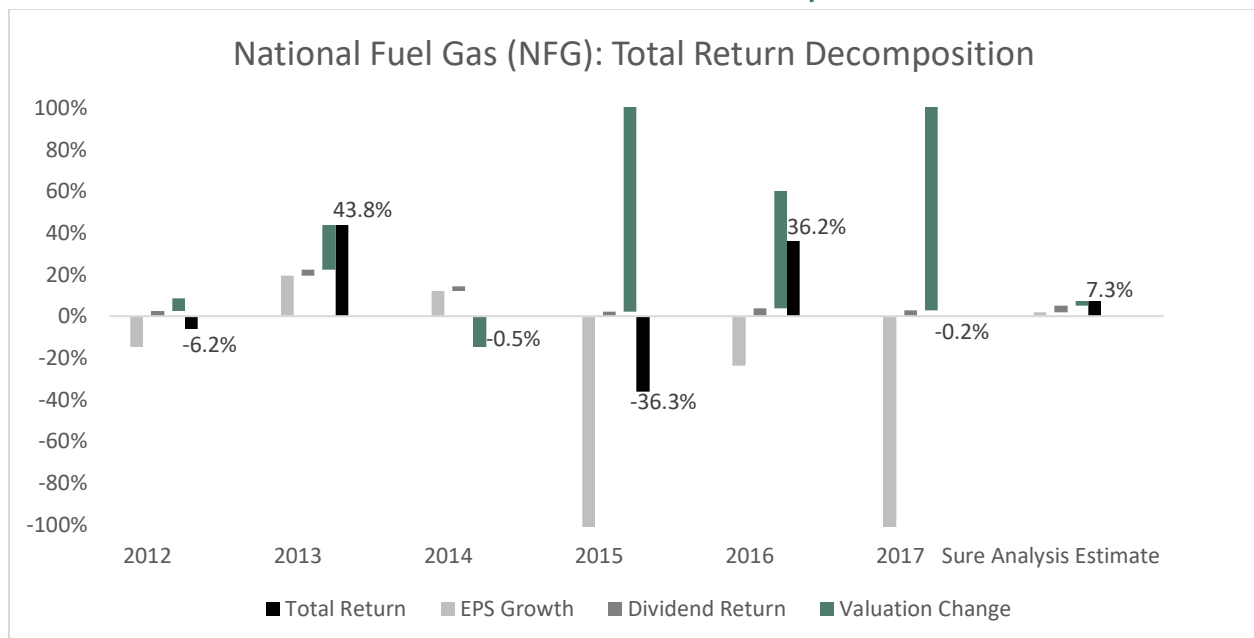
National Fuel Gas has a healthy balance sheet while its interest coverage level stands at a decent level, around 6.0. Moreover, its dividend payout ratio is sufficiently low to enable continued dividend growth even if earnings stall temporarily. Management has always targeted a dividend payout ratio around 50% in order to have a high margin of safety against the wide fluctuations of the price of natural gas. As the 3.0% dividend yield of National Fuel Gas is much higher than the yield of S&P (1.9%), the stock may entice income-oriented investors. However, the latter should be aware of the high dependence of the earnings of the company on the price of natural gas.

Qualitatively, National Fuel Gas' competitive advantage is its combination of regulated and stable businesses (like pipelines and utilities) with cyclical and (potentially) higher-growth sectors (like exploration & production). This allows the company to endure through difficult operating environments with less difficulty than its peers who may focus exclusively on the more cyclical areas of the energy sector.

## Final Thoughts & Recommendation

Thanks to a rising natural gas price, production growth, and lower operating costs, National Fuel Gas is likely to offer a 7.3% average annual return over the next five years. However, this return is lackluster, particularly given the poor financial performance of the company in recent years and its heavy dependence on the price of natural gas. National Fuel Gas fails is a hold at current prices.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue</b>	2052	1761	1779	1627	1830	2113	1761	1452	1580	1593
<b>Gross Profit</b>	1054	1102	924	940	1042	935	891	895	935	873
<b>Gross Margin</b>	51.4%	62.6%	51.9%	57.8%	57.0%	44.2%	50.6%	61.6%	59.2%	54.8%
<b>Operating Profit</b>	410	440	441	448	518	570	515	532	553	487
<b>Operating Margin</b>	20.0%	25.0%	24.8%	27.5%	28.3%	27.0%	29.3%	36.6%	35.0%	30.6%
<b>Net Profit</b>	101	226	258	220	260	299	-379	-291	283	392
<b>Net Margin</b>	4.9%	12.8%	14.5%	13.5%	14.2%	14.2%	-21.5%	-20.0%	17.9%	24.6%
<b>Free Cash Flow</b>	298	4	-160	-376	35	-5	-165	7	234	30
<b>Income Tax</b>	53	137	164	151	173	190	-319	-233	161	-7

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	4769	5106	5221	5935	6218	6728	6565	5636	6103	6036
<b>Cash &amp; Equivalents</b>	408	397	80	N/A	N/A	N/A	N/A	N/A	N/A	N/A
<b>Accounts Receivable</b>	144	163	163	116	133	150	105	133	112	141
<b>Inventories</b>	80	74	82	78	94	67	65	71	74	78
<b>Goodwill &amp; Int. Ass.</b>	27	5	5	5	5	5	5	5	5	5
<b>Total Liabilities</b>	3180	3360	3329	3975	4024	4317	4539	4109	4400	4099
<b>Accounts Payable</b>	197	128	142	88	105	137	180	108	126	160
<b>Long-Term Debt</b>	1249	1249	1089	1570	1649	1723	2084	2086	2384	2131
<b>Shareholder's Equity</b>	1589	1746	1892	1960	2195	2411	2025	1527	1704	1937
<b>D/E Ratio</b>	0.79	0.72	0.58	0.80	0.75	0.71	1.03	1.37	1.40	1.10

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	2.3%	4.6%	5.0%	3.9%	4.3%	4.6%	-5.7%	-4.8%	4.8%	6.5%
<b>Return on Equity</b>	6.3%	13.5%	14.2%	11.4%	12.5%	13.0%	-17.1%	-16.4%	17.5%	21.5%
<b>ROIC</b>	3.6%	7.7%	8.6%	6.8%	7.1%	7.5%	-9.2%	-7.5%	7.4%	9.6%
<b>Shares Out.</b>	80.5	82.1	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0
<b>Revenue/Share</b>	25.44	21.30	21.26	19.43	21.69	24.87	20.87	17.12	18.37	18.43
<b>FCF/Share</b>	3.70	0.05	-1.92	-4.49	0.42	-0.06	-1.95	0.09	2.72	0.34

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

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