



National Fuel Gas Co. (NFG)

Updated August 9th, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	\$49	5 Year CAGR Estimate:	10.4%	Volatility Percentile:	20.7%
Fair Value Price:	\$63	5 Year Growth Estimate:	2.0%	Momentum Percentile:	29.6%
% Fair Value:	79%	5 Year Valuation Multiple Estimate:	4.9%	Growth Percentile:	8.3%
Dividend Yield:	3.5%	5 Year Price Target	\$69	Valuation Percentile:	86.4%
Dividend Risk Score:	C	Retirement Suitability Score:	C	Total Return Percentile:	64.6%

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 \$4.2 billion. With 49 years of consecutive dividend increases, National Fuel Gas qualifies to be a Dividend Champion.

In early August, National Fuel Gas reported (8/1/19) financial results for the third quarter of fiscal 2019. The company benefited from 23% production growth but was hurt by a 3% decrease in average price of natural gas over last year's quarter, after the effect of hedging. Moreover, the results of the E&P segment were affected by higher taxes while the midstream segment incurred higher operation and maintenance expenses. Overall, adjusted earnings-per-share fell from \$0.73 to \$0.71 but exceeded analysts' consensus by \$0.05.

Management reduced its guidance for the earnings-per-share of this fiscal year from \$3.45-\$3.65 to \$3.40-\$3.50 due to lower natural gas prices. We have thus lowered our forecast for this year from \$3.51 to \$3.45. Moreover, management provided guidance for earnings-per-share between \$3.25 and \$3.55 in fiscal 2020, as it expects the increased production of natural gas to be offset by lower prices and increased operating expenses.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$2.60	\$2.65	\$3.09	\$2.63	\$3.14	\$3.52	-\$4.50	-\$3.43	\$3.30	\$3.34	\$3.45	\$3.81
DPS	\$1.32	\$1.36	\$1.40	\$1.44	\$1.48	\$1.52	\$1.56	\$1.60	\$1.64	\$1.68	\$1.72	\$1.92
Shares	80.5	82.1	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0	87.0	90.0

National Fuel gas pursues growth by growing its natural gas production and expanding its pipeline network. However, 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 \$3.81.

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
Avg. P/E	15.5	13.4	18.5	21.4	19.3	18.6	20.6	---	---	17.2	14.2	18.0
Avg. Yld.	2.6%	3.8%	2.8%	2.1%	2.8%	2.5%	2.1%	2.5%	3.1%	2.9%	3.5%	2.8%

National Fuel Gas is trading at a price-to-earnings ratio of 14.2. 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

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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 4.9% 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%	---	---	49.7%	50.3%	49.9%	50.4%

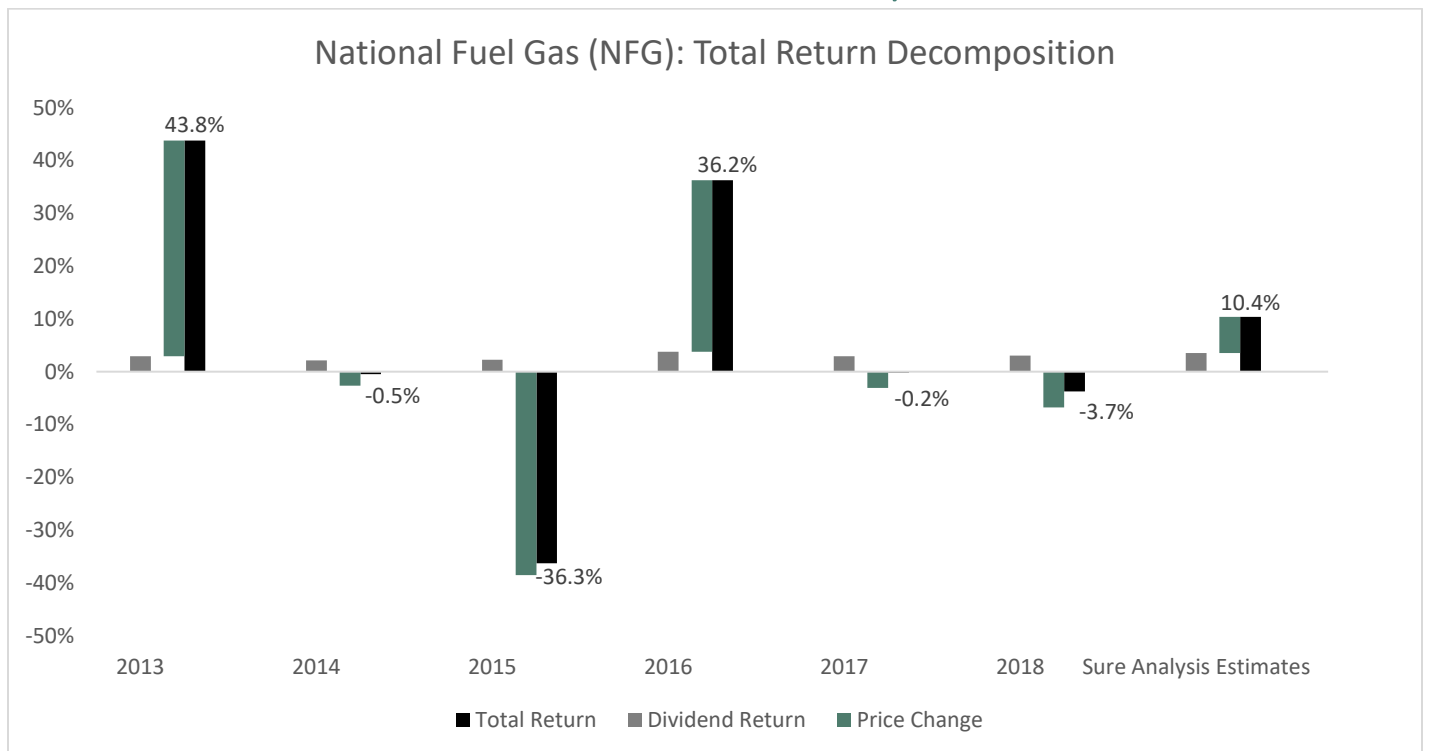
National Fuel Gas has a healthy balance sheet while its interest coverage level stands at a decent level, around 6.0. Moreover, its dividend payout ratio is sufficiently low to enable continued dividend growth even if earnings stall temporarily. Management has always targeted a dividend payout ratio around 50% in order to have a high margin of safety against the wide fluctuations of the price of natural gas. As the 3.5% 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, these investors should be aware of the company's high dependence 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 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 its sustained production growth and the 20% decline of its stock price in the last four months, National Fuel Gas could offer a 10.4% average annual return over the next five years. However, this return expectation is lackluster, particularly given the poor financial performance of the company in recent years and its heavy dependence on the price of natural gas. We rate National Fuel Gas as 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
Revenue	2052	1761	1779	1627	1830	2113	1761	1452	1580	1593
Gross Profit	1054	1102	924	940	1042	935	891	895	935	873
Gross Margin	51.4%	62.6%	51.9%	57.8%	57.0%	44.2%	50.6%	61.6%	59.2%	54.8%
Operating Profit	410	440	441	448	518	570	515	532	553	487
Operating Margin	20.0%	25.0%	24.8%	27.5%	28.3%	27.0%	29.3%	36.6%	35.0%	30.6%
Net Profit	101	226	258	220	260	299	-379	-291	283	392
Net Margin	4.9%	12.8%	14.5%	13.5%	14.2%	14.2%	-21.5%	-20.0%	17.9%	24.6%
Free Cash Flow	298	4	-160	-376	35	-5	-165	7	234	30
Income Tax	53	137	164	151	173	190	-319	-233	161	-7

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	4769	5106	5221	5935	6218	6728	6565	5636	6103	6036
Cash & Equivalents	408	397	80	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Accounts Receivable	144	163	163	116	133	150	105	133	112	141
Inventories	80	74	82	78	94	67	65	71	74	78
Goodwill & Int. Ass.	27	5	5	5	5	5	5	5	5	5
Total Liabilities	3180	3360	3329	3975	4024	4317	4539	4109	4400	4099
Accounts Payable	197	128	142	88	105	137	180	108	126	160
Long-Term Debt	1249	1249	1089	1570	1649	1723	2084	2086	2384	2131
Shareholder's Equity	1589	1746	1892	1960	2195	2411	2025	1527	1704	1937
D/E Ratio	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
Return on Assets	2.3%	4.6%	5.0%	3.9%	4.3%	4.6%	-5.7%	-4.8%	4.8%	6.5%
Return on Equity	6.3%	13.5%	14.2%	11.4%	12.5%	13.0%	-17.1%	-16.4%	17.5%	21.5%
ROIC	3.6%	7.7%	8.6%	6.8%	7.1%	7.5%	-9.2%	-7.5%	7.4%	9.6%
Shares Out.	80.5	82.1	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0
Revenue/Share	25.44	21.30	21.26	19.43	21.69	24.87	20.87	17.12	18.37	18.43
FCF/Share	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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