Spark Energy Inc. (SPKE)

Updated March 6th, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	$8.90	**5 Year CAGR Estimate:**	6.9%	**Market Cap:**	$311 M
Fair Value Price:	$3.10	**5 Year Growth Estimate:**	22.9%	**Ex-Dividend Date:**	2/28/2020
% Fair Value:	285%	**5 Year Valuation Multiple Estimate:**	-18.9%	**Dividend Payment Date:**	3/16/2020
Dividend Yield:	8.2%	**5 Year Price Target**	$8.80	**Years Of Dividend Growth:**	0
Dividend Risk Score:	F	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	N/A

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 $311 million and executed its initial public offering in 2014.

In early March, Spark Energy reported (3/4/20) financial results for the fourth quarter of fiscal 2019. In the year, its adjusted EBITDA grew 31%, from $70.7 million to $92.4 million, and its retail gross margin rose from $185.1 million to $220.7 million thanks to higher electricity unit margins, which were partly offset by a lower customer count. The company improved its customer portfolio, as it continued to shed low-margin customers in favor of high-margin customers. In addition, it benefited from its hedging strategy. While Spark Energy significantly improved its earnings, it still made a profit of only $0.02 per share in the full year, as nearly all its earnings were spent on the dividends of its preferred shares.

Spark Energy does not provide any guidance for the year. We note the positive business momentum of the company and the fact that it has left most of its litigation issues behind, as it settled them last year. Nevertheless, due to the opaque business model of Spark Energy and its volatile record, we expect earnings-per-share around $0.25 this year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	---	---	---	---	-$0.01	$0.53	$1.11	$1.21	-$0.69	$0.02	***$0.25***	***$0.70***
DPS	---	---	---	---	$0.30	$0.73	$0.73	$0.73	$0.73	$0.73	***$0.73***	***$0.73***
Shares[1]	---	---	---	---	6.00	6.24	33.44	34.62	34.99	35.0	***35.0***	***40.0***

Since its IPO, Spark Energy has made 14 acquisitions and has grown its customer base at a fast pace. However, this strategy has not borne fruit yet. The company has a remarkably volatile performance record and hence it is essentially impossible to forecast its future results with any degree of accuracy. Its fragile business model is also evident from the markedly high monthly attrition rate, which averaged 5.0% in 2019. Spark Energy posted a loss in 2018 and a marginal profit last year while it has not provided any material guidance for this year. It is also worth noting that Spark Energy offers very little information in its earnings reports and is hardly followed by analysts. It is also concerning that its management remains focused on EBITDA instead of earnings. We prefer to be conservative and expect earnings-per-share around $0.70 in 2025.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	---	---	---	---	---	14.7	12.0	13.5	---	---	***35.6***	***12.5***
Avg. Yld.	---	---	---	---	---	9.3%	5.5%	4.5%	7.6%	7.4%	***8.2%***	***8.3%***

[1] In millions.

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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. Due to the depressed earnings expected this year, the stock is trading at a price-to-earnings ratio of 35.6 right now. If Spark Energy's price-to-earnings ratio contracts to 12.5 over the next five years, the stock would incur a -18.9% annualized drag, which will offset most of its 22.9% expected annual earnings-per-share growth off its low base this year.

Safety, Quality, Competitive Advantage, & Recession Resiliency

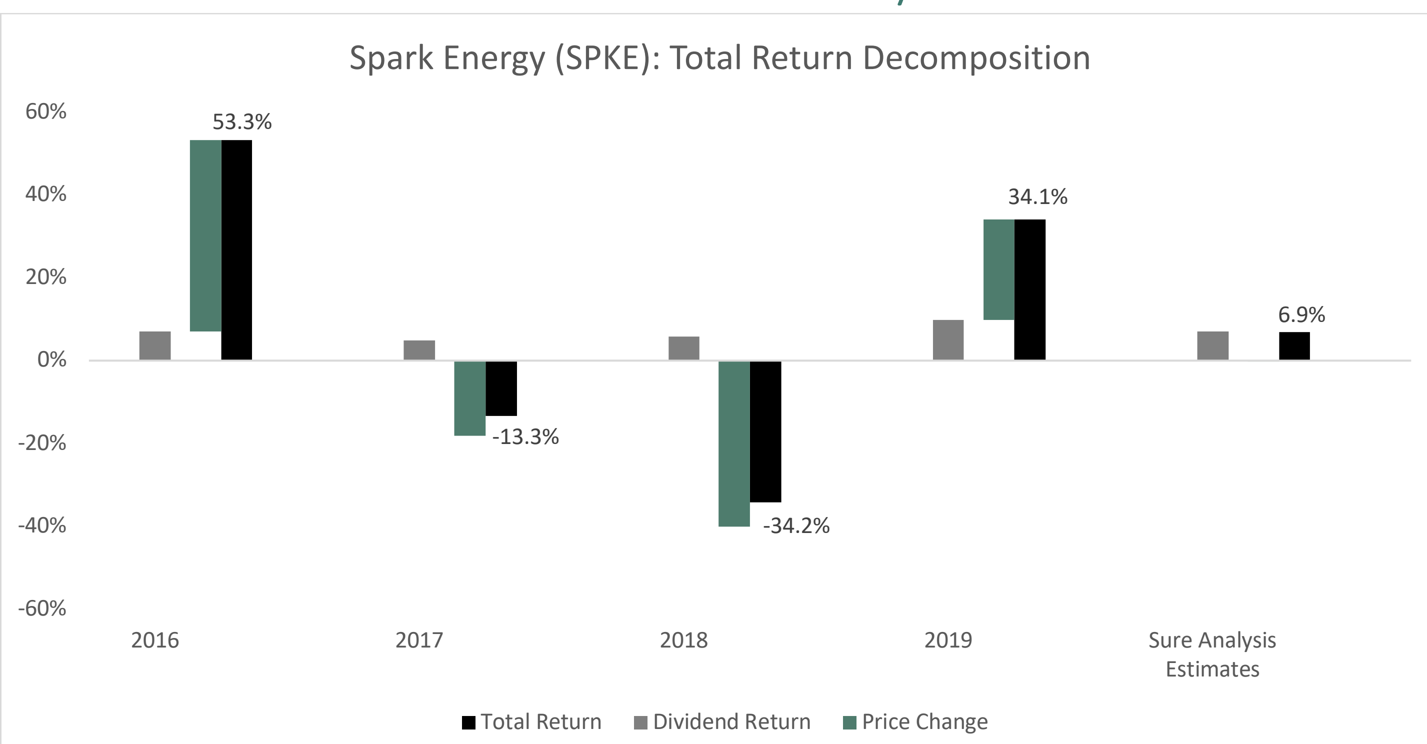
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	---	---	---	138%	65.8%	61.3%	---	3650%	***292%***	***104%***

As a small-cap energy business, Spark Energy tends to be more volatile than most large cap stocks. To provide a perspective, the stock is -75% off its peak posted almost three years ago. Moreover, the stock is likely to underperform the market whenever the next bear market shows up. This is evident in the ongoing correction of the market, in which the stock has shed -15% whereas the S&P has lost only -10%. Furthermore, Spark Energy is hardly followed by analysts and provides little information in its reports.

Final Thoughts & Recommendation

Spark Energy has incurred a -15% correction in less than a month, primarily due to the broad market sell-off that has resulted from the coronavirus. However, the stock is still far from attractive. We expect it to offer just a 6.9% average annual return over the next five years, mostly thanks to its 8.2% dividend yield. As the company has begun to improve its performance, it may offer higher returns but management provides too little information on the results and no guidance. Also, given the markedly volatile performance record of Spark Energy, the stock is highly speculative. Moreover, retirees should note that Spark Energy earns a poor rating for Retirement Suitability, largely due to its short dividend history and its excessive payout ratio. We rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	N/A	N/A	N/A	317	323	358	547	798	1006
Gross Profit	N/A	N/A	N/A	84	64	117	202	246	160
Gross Margin	N/A	N/A	N/A	26.5%	19.9%	32.7%	36.9%	30.8%	15.9%
SG&A Exp.	N/A	N/A	N/A	35	46	62	85	101	111
D&A Exp.	N/A	N/A	N/A	16	22	25	49	43	51
Operating Profit	N/A	N/A	N/A	33	-4	30	84	102	-4
Operating Margin	N/A	N/A	N/A	10.4%	-1.2%	8.3%	15.4%	12.8%	-0.4%
Net Profit	N/A	N/A	N/A	31	0	4	14	19	-1
Net Margin	N/A	N/A	N/A	9.9%	0.0%	1.1%	2.6%	2.4%	-0.1%
Free Cash Flow	N/A	N/A	N/A	43	3	44	65	60	58
Income Tax	N/A	N/A	N/A	0	-1	2	10	39	2

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	N/A	N/A	N/A	109	138	162	375	504	489
Cash & Equivalents	N/A	N/A	N/A	11	4	4	19	29	41
Accounts Receivable	N/A	N/A	N/A	63	65	62	112	162	153
Inventories	N/A	N/A	N/A	4	8	4	4	4	4
Goodwill & Int. Ass.	N/A	N/A	N/A	0	4	29	101	155	147
Total Liabilities	N/A	N/A	N/A	73	114	129	251	303	308
Accounts Payable	N/A	N/A	N/A	37	39	30	52	82	72
Long-Term Debt	N/A	N/A	N/A	28	33	49	78	146	146
Shareholder's Equity	N/A	N/A	N/A	36	9	11	30	58	46
D/E Ratio	N/A	N/A	N/A	0.77	3.81	4.30	2.58	1.48	1.07

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	N/A	N/A	N/A	26.4%	0.0%	2.6%	5.4%	4.4%	-0.2%
Return on Equity	N/A	N/A	N/A	64.6%	-0.2%	38.7%	69.3%	43.8%	-2.3%
ROIC	N/A	N/A	N/A	46.6%	-0.1%	5.6%	10.2%	7.0%	-0.4%
Shares Out.	N/A	N/A	N/A	6.00	6.24	33.44	34.62	34.99	6.00
Revenue/Share	N/A	N/A	N/A	18.93	53.81	53.82	43.08	59.80	75.13
FCF/Share	N/A	N/A	N/A	2.57	0.47	6.64	5.10	4.53	4.36

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