



TC Energy Corporation (TRP)

Updated August 31st, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	\$48	5 Year CAGR Estimate:	9.7%	Market Cap:	\$45.0 B
Fair Value Price:	\$51	5 Year Growth Estimate:	4.0%	Ex-Dividend Date:	9/25/2020 ¹
% Fair Value:	94%	5 Year Valuation Multiple Estimate:	1.3%	Dividend Payment Date:	10/29/2020
Dividend Yield:	5.0%	5 Year Price Target	\$62	Years Of Dividend Growth:	5
Dividend Risk Score:	D	Retirement Suitability Score:	C	Last Dividend Increase:	8.0%

Overview & Current Events

On May 3rd, 2019, TransCanada Corporation changed its name to TC Energy Corporation. TC Energy Corporation operates Canada's largest natural gas pipeline system. The company owns more than 57,000 miles of natural gas pipelines and more than 3,000 miles of liquids pipelines. TC Energy Corporation operates through three segments: Natural Gas Pipelines, Oil Pipelines, and Energy. The Natural Gas Pipelines segment generated 66% of consolidated revenue in the most recent fiscal year. TC Energy Corporation is headquartered in Calgary, Alberta, Canada, and its common shares are cross listed on both the Toronto Stock Exchange and the New York Stock Exchange, where they trade with a market capitalization of US\$45 billion. In this report, all figures are reported in U.S. dollars.

In late July, TC Energy reported (7/30/20) financial results for the second quarter of fiscal 2020. The energy market is going through a downturn due to the pandemic, but the natural gas market has proved more resilient than the oil market. In addition, TC Energy is largely insulated from the downturn thanks to its regulated assets and its long-term contracts, which generate 95% of its EBITDA. As a result, its flows and utilization rates remained in line with historical levels and its adjusted earnings-per-share fell only -8% over last year's quarter. Due to the markedly resilient performance of TC Energy, we have restored our initial earnings-per-share forecast for the year, from \$2.90 to \$3.20.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$1.77	\$2.12	\$1.84	\$2.28	\$2.12	-\$1.26	\$0.12	\$2.38	\$2.97	\$3.18	\$3.20	\$3.89
DPS	\$1.60	\$1.65	\$1.76	\$1.73	\$1.66	\$1.50	\$1.68	\$1.99	\$2.12	\$2.31	\$2.40	\$3.06
Shares²	696.2	704.0	705.0	707.0	709.0	702.6	863.8	881.4	918.0	938.0	950.0	1,100.0

TC Energy's growth strategy has been to raise capital (in the form of either debt or equity) to fund growth projects. Over the last decade, until 2017, this strategy failed to generate meaningful growth for the company *on a per-share basis*, as the additional net income generated by these projects was offset by the increased share count.

However, we believe that the next several years will show an improvement for TC Energy thanks to a strong pipeline of growth projects. TC Energy has more than \$20 billion of growth projects underway. These projects are supported by regulated or long-term contracted business models. Management expects earnings and cash flows to continue to grow in the upcoming years. We expect 4% annualized growth over the next five years. Management has guided for 8%-10% dividend growth in 2021 and 5%-7% dividend growth per year thereafter, though the high leverage is a concern.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	20.1	19.4	23.9	20.2	22.5	---	---	24.2	14.3	15.1	15.0	16.0
Avg. Yld.	4.5%	4.0%	4.0%	3.8%	3.5%	3.8%	4.0%	4.1%	5.0%	4.8%	5.0%	4.9%

¹ Estimated date.

² In millions.

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Excluding 2015 and 2016, when the company's earnings were depressed, TC Energy has traded at an average price-to-earnings ratio of 20.0 over the last decade. The stock is currently trading at a price-to-earnings ratio of 15.0, which is lower than our assumed fair price-to-earnings ratio of 16.0. If the stock reverts to our fair value estimate over the next five years, it will enjoy a 1.3% annualized gain thanks to the expansion of its valuation level.

Safety, Quality, Competitive Advantage, & Recession Resiliency

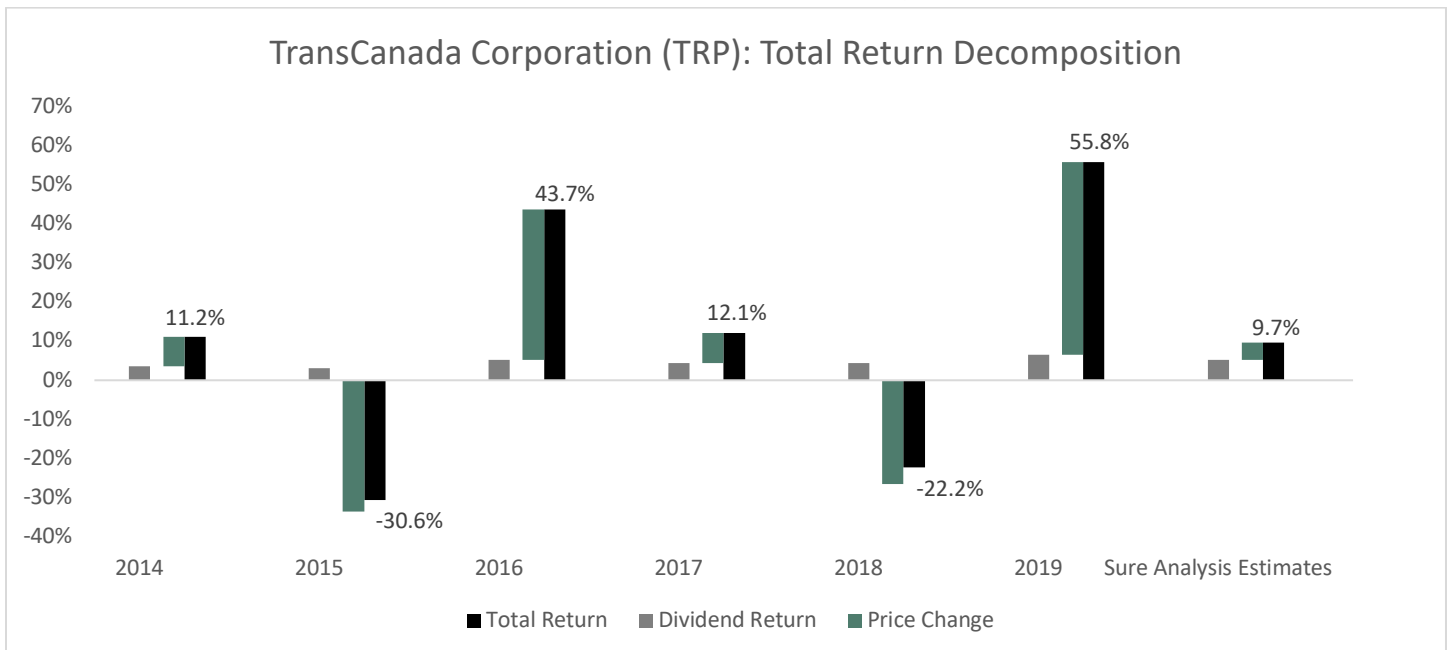
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	90.4%	77.8%	95.7%	75.9%	78.3%	---	---	83.6%	71.4%	72.5%	75.0%	78.7%

TC Energy has been investing heavily in growth projects in the last decade and will continue to do so in the years ahead. Consequently, it has posted negative free cash flows in 9 out of the last 10 years and has a leveraged balance sheet, with interest coverage of only 2.5x and net debt that is about 15 *times its earnings*. The company is exposed to unforeseen headwinds, such as a downturn in the energy market or a recession. In addition, as it often issues new shares, it dilutes its shareholders at a high rate whenever its stock declines. On the other hand, despite its high payout ratio, the stock is not likely to cut its dividend anytime soon thanks to the strong momentum in its business and the increasing contribution of new projects to its cash flows. TC Energy also seems fairly resilient in the ongoing recession, which has hurt the natural gas market much less than the oil market.

Final Thoughts & Recommendation

TC Energy Corporation has maintained its strong business performance amid the pandemic. Moreover, as we expect the pandemic to subside from next year, the stock could offer a 9.7% average annual return over the next five years thanks to its 5.0% dividend yield, 4.0% annual earnings-per-share growth and a modest expansion of its valuation level. For yield-hungry investors looking for exposure to the energy sector, we believe the company is a hold, on the verge of earning a buy rating. However, due to its high leverage, its negative free cash flows and its tendency to dilute shareholders, investors should take caution. There are other opportunities within the energy sector, such as Exxon Mobil and Total, which have good return prospects at current prices and a much less risky profile.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	6,643	7,928	8,009	8,543	9,226	8,895	9,475	10,377	10,556	9,987
Gross Profit	2,371	3,198	3,007	3,225	3,410	3,172	3,455	3,940	4,823	4,907
Gross Margin	35.7%	40.3%	37.5%	37.8%	37.0%	35.7%	36.5%	38.0%	45.7%	49.1%
D&A Exp.	1,125	1,343	1,375	1,442	1,459	1,383	1,464	1,586	1,813	1,857
Operating Profit	1,875	2,783	2,573	2,793	2,982	2,767	3,036	3,501	4,384	4,359
Operating Margin	28.2%	35.1%	32.1%	32.7%	32.3%	31.1%	32.0%	33.7%	41.5%	43.7%
Net Profit	1,239	1,599	1,354	1,734	1,667	(898)	176	2,436	2,857	3,119
Net Margin	18.7%	20.2%	16.9%	20.3%	18.1%	-10.1%	1.9%	23.5%	27.1%	31.2%
Free Cash Flow	(1,454)	1,186	973	(1,047)	(101)	(35)	(176)	(1,774)	(2,592)	(829)
Income Tax	375	582	466	593	753	27	266	(69)	333	568

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	46,582	46,369	48,648	50,619	50,415	46,406	65,307	68,470	72,627	76,002
Cash & Equivalents	764	641	554	871	421	613	754	866	327	1,028
Acc. Receivable	1,271	1,072	1,057	1,054	1,131	999	1,539	2,006	1,861	1,854
Inventories	425	243	225	236	252	233	273	301	316	346
Goodwill & Int.	5,595	3,881	3,888	4,312	4,817	4,933	11,906	10,879	11,181	11,178
Total Liabilities	28,700	28,484	30,216	31,708	32,624	33,324	46,036	47,086	49,872	51,201
Accounts Payable	2,243	682	928	813	1,399	1,085	1,812	2,264	2,367	2,537
Long-Term Debt	21,862	21,097	22,297	24,202	24,451	25,282	33,269	34,601	36,887	38,200
Total Equity	15,501	15,251	15,769	15,695	14,485	10,045	15,039	16,747	18,618	20,503
D/E Ratio	1.31	1.28	1.31	1.39	1.49	2.13	1.85	1.74	1.71	1.62

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.8%	3.4%	2.9%	3.5%	3.3%	-1.9%	0.3%	3.6%	4.0%	4.2%
Return on Equity	8.3%	10.4%	8.7%	11.0%	11.0%	-7.3%	1.4%	15.3%	16.2%	15.9%
ROIC	3.3%	4.1%	3.4%	4.1%	3.9%	-2.2%	0.4%	4.5%	4.9%	5.1%
Shares Out.	696.2	704.0	705.0	707.0	709.0	702.6	863.8	881.4	918.0	938.0
Revenue/Share	9.60	11.28	11.34	12.07	12.99	12.55	12.47	11.87	11.69	10.73
FCF/Share	(2.10)	1.69	1.38	(1.48)	(0.14)	(0.05)	(0.23)	(2.03)	(2.87)	(0.89)

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

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