Duke Energy Corporation (DUK)

Updated November 11th, 2020 by Samuel Smith

Key Metrics

Current Price:	$97	**5 Year CAGR Estimate:**	3.8%	**Market Cap:**	$71.5B
Fair Value Price:	$76	**5 Year Growth Estimate:**	4.7%	**Ex-Dividend Date:**	11/12/20
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.7%	**Dividend Payment Date:**	12/16/20
Dividend Yield:	4.0%	**5 Year Price Target**	$96	**Years Of Dividend Growth:**	9
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	2.1%

Overview & Current Events

Duke Energy began operations in 1904 by providing power to a South Carolina cotton mill. Since that time, it has grown both organically and through mergers to become one of the largest providers of energy in the US. Today, it produces $25.5 billion in annual revenue and trades with a market capitalization of $71.5 billion.

On November 5th, Duke Energy reported Q3 earnings. Q3 adjusted earnings grew to $1.87 per share from 2019 Q3's $1.79 in earnings-per-share. Thanks to new projects coming online, DUK income from commercial renewables grew 50% from $40 million to $60 million. On the other hand, power sales across its six-state electric utilities fell from 73,931 GWh in 2019 to 70,875 GWh, some of which can be attributed to weather-related reasons, specifically in the Southeast. One factor that helped reduce the impact of lower sales was controlling the operations and maintenance costs, which gave an additional $0.08 boost to EPS. The company also updated its guidance for FY 2020, eyeing EPS of $5.05-$5.20 compared to its previous guidance of $5.05-$5.45 and the analyst consensus estimate of $5.08.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$4.02	$4.14	$3.71	$3.98	$4.13	$4.10	$3.71	$4.22	$4.72	$5.06	***$5.09***	***$6.39***
DPS	$2.91	$2.97	$3.03	$3.09	$3.15	$3.24	$3.36	$3.49	$3.60	$3.71	***$3.86***	***$4.50***
Shares[1]	443	445	704	706	707	688	700	700	705	730	***730***	***775***

Duke's earnings-per-share have increased at an annual rate of 4% over the last decade, and we expect to see Duke continuing to generate 4.7% annual earnings-per-share growth over the next half decade. This is near the middle of management's guidance for 4%-6% growth through 2023. That is because the key determiners of Duke's value proposition to investors will be how well they can execute on their ambitious $37 billion growth CapEx plan, and if they can continue to garner favorable regulatory rulings in their operating regions. While they continue to achieve reasonable regulatory rulings, there are no guarantees this will continue, especially if government energy policies shift with 2020 election results. Even more concerning are the problems and cost overruns being experienced with the Atlantic Coast Pipeline project thus far, indicating that returns on Duke's projected capex may not be as high as forecast. We therefore take a cautious and conservative outlook on growth, projecting Duke achieving the low end of its guidance.

That being said, customer growth should continue as a low-single-digit tailwind for the foreseeable future, providing Duke with ever-higher base demand for its services. Of course, the weather can have a significant impact positively or negatively in any particular year, but overall, a low-single-digit tailwind from customer growth is very likely. In addition, rate increases should help boost revenue and earnings, as we've seen with Duke's recent rate increases in North Carolina and Kentucky. Duke, like any other power provider, must ask for rate increases from local authorities so they are certainly not assured. However, state regulators have been amicable to rate increase requests from Duke and should continue to be moving forward. One offsetting factor in earnings-per-share growth is that Duke likes to issue common stock for general corporate purposes, leading to a higher share count over time. Its share count has risen from 424 million in 2008 to more than 730 million today. Share issuances are irregularly timed and sized so the exact impact is

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[1] Share count in millions

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difficult to predict, but this is a long-term habit for Duke and must be accounted for in estimates. The dividend continues to rise at a low-single-digit pace, slightly under that of earnings-per-share growth. We expect this will continue, keeping Duke firmly in the income stock category. We see dividend growth roughly keeping pace with growth in the share price.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.3	12.7	13.8	17.5	17.4	17.9	18.2	21.3	19.9	18.6	***19.1***	***15.0***
Avg. Yld.	6.2%	5.7%	5.2%	4.7%	4.4%	4.3%	4.3%	4.3%	4.2%	4.2%	***3.9%***	***4.7%***

Duke's valuation has remained mostly steady throughout the past decade, with the exception of the period immediately following the Great Recession. Duke's price-to-earnings ratio has averaged 17 over the past decade, but given current headwinds, we are reducing the fair value to 15 times earnings. Today's price-to-earnings ratio of 19.1 is above our reduced fair value estimate, and we therefore see a headwind to annual total returns from a contracting multiple over time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

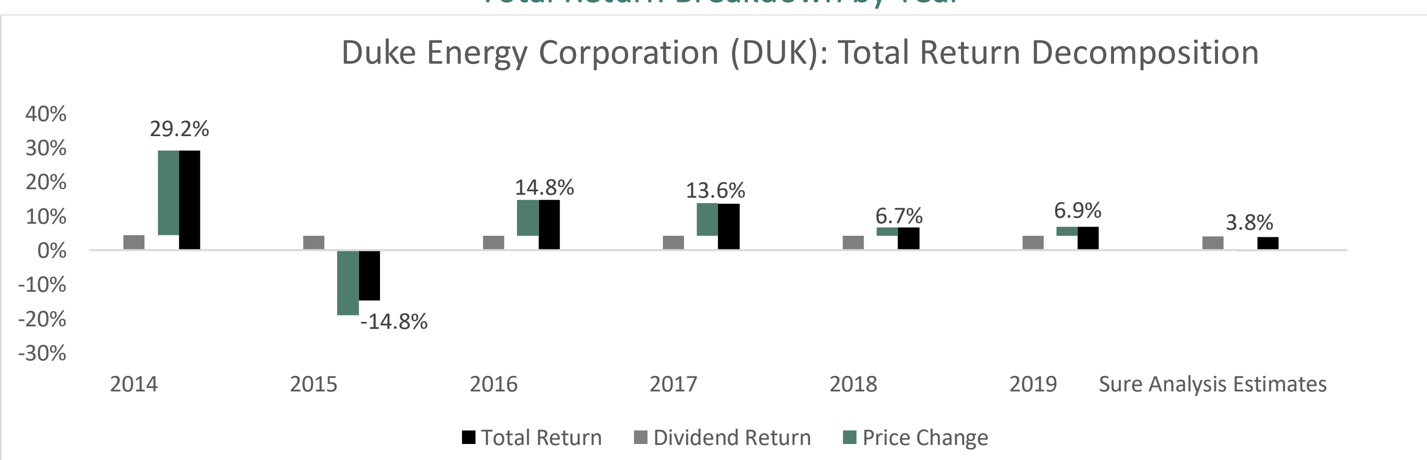
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	84%	73%	72%	82%	78%	76%	79%	91%	83%	76%	***76%***	***70%***

Duke's quality metrics have been largely stable throughout the past decade and we do not expect that will change. We expect margins to be flat moving forward – albeit at very high levels – and for its balance sheet leverage and interest coverage to remain steady. Management has a stated plan to reduce leverage moving forward as it plans to boost cash flow against the amount of debt it takes on, so we are not concerned. The payout ratio is relatively high, but the dividend is well-covered, and should be for the foreseeable future. Duke's competitive advantage is its near monopoly in the areas it serves, which is not dissimilar to other regulated utilities. In addition, recession performance should be excellent as it grew earnings-per-share rather rapidly during the Great Recession, making this is a truly defensive stock with a high yield and decent growth prospects.

Final Thoughts & Recommendation

We expect Duke to produce 3.8% total annual returns from its 3.9% current yield and 4.7% expected earnings-per-share growth, partially offset by a headwind from multiple contraction. Its highly defensive business model should position it well to weather current uncertainty from the coronavirus pandemic and any recession or depression to follow. We therefore rate it a hold at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	14272	14529	17912	22756	22509	22371	22743	23565	24521	25079
Gross Profit	5522	5614	6677	9211	9086	9336	9629	10639	10530	11560
Gross Margin	38.7%	38.6%	37.3%	40.5%	40.4%	41.7%	42.3%	45.1%	42.9%	46.1%
D&A Exp.	1994	2026	2652	3229	3507	3613	3880	4046	4696	5176
Operating Profit	3034	3104	3567	5269	4913	5154	5193	5879	5176	5705
Op. Margin	21.3%	21.4%	19.9%	23.2%	21.8%	23.0%	22.8%	24.9%	21.1%	22.7%
Net Profit	1320	1706	1768	2665	1883	2816	2152	3059	2666	3748
Net Margin	9.2%	11.7%	9.9%	11.7%	8.4%	12.6%	9.5%	13.0%	10.9%	14.9%
Free Cash Flow	(292)	(691)	(257)	856	1202	(66)	(1038)	(1428)	(2203)	(2913)
Income Tax	890	752	623	1205	1225	1256	1156	1196	448	519

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets ($B)	59090	62526	113856	114779	120557	121156	132761	137914	145392	158838
Cash & Equivalents	1670	2110	1424	1501	2036	383	392	358	442	311
Acc. Receivable	764	1941	2717	3005	2764	2263	2644	2774	3134	3060
Inventories	1318	1588	3223	3250	3459	3746	3522	3250	3084	3232
Goodwill & Int.	4325	4212	16365	16340	16321	16072	19425	19396	19303	19303
Total Liab. ($B)	36437	39661	72822	73371	79658	81385	91720	96177	101558	110887
Accounts Payable	1387	1433	2444	2391	2271	2350	2994	3043	3487	3487
Long-Term Debt	18426	21000	40518	41095	42382	42501	50382	54442	56998	60292
Total Equity	22522	22772	40863	41330	40875	39727	41033	41739	43817	44860
D/E Ratio	0.82	0.92	0.99	0.99	1.04	1.07	1.23	1.30	1.30	1.29

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.3%	2.8%	2.0%	2.3%	1.6%	2.3%	1.7%	2.3%	1.9%	2.5%
Return on Equity	6.0%	7.5%	5.6%	6.5%	4.6%	7.0%	5.3%	7.4%	6.2%	8.5%
ROIC	3.3%	4.0%	2.8%	3.2%	2.3%	3.4%	2.5%	3.3%	2.7%	3.6%
Shares Out.	443	445	704	706	707	688	700	700	705	730
Revenue/Share	32.44	32.72	31.15	32.23	31.84	32.23	32.91	33.66	34.63	34.40
FCF/Share	(0.66)	(1.56)	(0.45)	1.21	1.70	(0.10)	(1.50)	(2.04)	(3.11)	(4.00)

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