Energy Transfer LP (ET)

Updated November 16th, 2020 by Samuel Smith

Key Metrics

Current Price:	$5.4	**5 Year CAGR Estimate:**	24.5%	**Market Cap:**	$14.4B
Fair Value Price:	$12.4	**5 Year Growth Estimate:**	-0.7%	**Ex-Dividend Date:**	2/5/21[1]
% Fair Value:	43%	**5 Year Valuation Multiple Estimate:**	18.1%	**Dividend Payment Date:**	2/19/21[2]
Dividend Yield:	11.3%	**5 Year Price Target**	$12.0	**Years Of Dividend Growth:**	0
Dividend Risk Score:	C	**Retirement Suitability Score:**	A	**Last Dividend Increase:**	NA

Overview & Current Events

On October 19th, 2018 Energy Transfer Equity, LP (previously ETE) and Energy Transfer Partners, LP (previously ETP) announced the completion of a merger with ETE buying ETP. As part of the merger, ETE changed its name to "Energy Transfer LP" and the common units began trading under the "ET" symbol. The combined firm owns and operates one of the largest and most diversified portfolios of energy assets in the United States. Operations include natural gas transportation and storage along with crude oil, natural gas liquids and refined product transportation and storage totaling 83,000 miles of pipelines. Energy Transfer, a $14.4 billion market capitalization company, also owns the Lake Charles LNG Company, as well as stakes in publicly traded Sunoco LP (SUN) and USA Compression Partners (USAC). On September 26th, management announced its acquisition of SemGroup in a $5 billion deal.

ET reported Q3 FY20 results on Nov 4th. The company reported a distributable cash flow of $1.69 billion, higher than Q3 2019 distributable cash flow of $1.55 billion. Adjusted EBITDA exceeded the $2.6 billion estimate at $2.87 billion. Management estimates that full-year 2020 adjusted EBITDA will come in at the high-end range of $10.2 – 10.5 billion vs the $10.34 billion consensus analyst estimate. ET forecasts total growth investments of $3.3 billion for 2020, down $100 million from previous guidance.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
CF/S	$0.73	$1.01	$0.91	$1.31	$2.12	$3.12	$3.20	$3.38	$2.06	$2.20	***$2.07***	***$2.00***
DPS	$0.54	$0.61	$0.63	$0.67	$0.80	$1.08	$1.14	$1.15	$1.22	$1.22	***$0.61***	***$1.00***
Units[3]	892	892	1,120	1,123	1,081	1,047	1,047	1,079	2,619	2,650	***2,650***	***2,650***

Energy Transfer operates a "toll booth" model of transporting energy, with natural gas being particularly interesting. Eventually the world may move away from fossil fuels, but for the foreseeable future that is not the case. In the meantime, natural gas is a cleaner, more efficient and often cheaper alternative – something we have seen play out in the last decade as U.S. electricity production has shifted dramatically away from coal and toward natural gas.

The partnership has a healthy backlog, with the expectation to spend billions of dollars in capital expenditures this year. However, the weak market in oil right now combined with plummeting demand from the coronavirus outbreak has caused us to forecast significant renegotiations for ET's contracts with clients and a corresponding decline in cash flows. As expected, warnings from the credit agencies forced management to reduce the distribution this year so they can better deleverage the balance sheet.

[1] Estimate
[2] Estimate
[3] Units in millions

Disclosure: This analyst is long the security discussed in this research report.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg P/DCF	13.4	10.0	12.5	15.6	13.5	4.4	6.0	5.1	6.4	5.3	***2.6***	***6.0***
Avg. Yld.	6.2%	6.1%	5.9%	4.3%	3.1%	4.0%	8.6%	6.5%	9.2%	10.5%	***11.3%***	***8.3%***

Notice that while Distributable Cash Flow per unit overall increased during the past decade despite a generous distribution policy, the valuation investors were willing to pay has declined dramatically despite interest rates also declining over the same period.

For instance, the share price tripled from the end of 2012 through mid-2015, before dropping ~80% in late 2015 / early 2016. We believe ~6 times distributable cash flow is a reasonable multiple for pipelines in general and Energy Transfer in particular, taking into consideration the decent growth profile and stable diversified business model offset by the higher leverage profile and the current headwinds facing the business. Investor returns will be largely driven by the exceptionally high distribution yield and massive multiple expansion over the next half decade.

Safety, Quality, Competitive Advantage, & Recession Resiliency

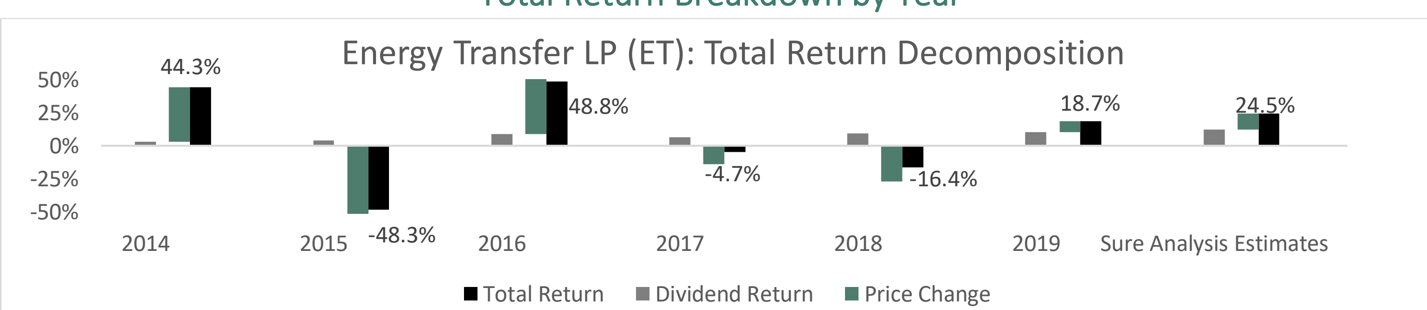
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	74%	60%	69%	51%	38%	35%	36%	34%	59%	56%	***29%***	***50%***

Energy Transfer is making strides in the safety department. Since the merger, Moody's revised its credit rating to stable (Baa3 investment grade) and the company has told investors that it anticipates funding the remainder of its growth capex with retained cash flow – reducing its reliance on the debt and capital markets. Today, the credit agency defined Debt-to-Adjusted EBITDA levels still remain above their desired range of 4.5x to 4.0x, but the partnership cut its distribution in half in order to retain billions of dollars per year in distributable cash flow for the express purpose of paying down debt faster. Additionally, Energy Transfer anticipates a distribution coverage ratio of nearly ~4x moving forward, which translates to a very conservative distribution payout ratio in the 25%-30% range. That is more or less typical for a growth-oriented company, but far lower than average for an MLP. That being said, there is considerable uncertainty hanging over the company right now due to plunging oil prices. As a result, the distribution and the balance sheet could be in danger if cash flows fall far enough due to contract defaults/renegotiations and threaten a downgrade to a junk credit rating.

Final Thoughts & Recommendation

Energy Transfer is a fairly risky bet given the current headwinds facing the space and its somewhat elevated leverage. That being said, in normal conditions the business model is quite safe and is somewhat recession resistant. Furthermore, units are selling at a very cheap price right now and the high distribution yield is covered nearly 4x by distributable cash flow, so we rate them a buy. However, conservative investors should maintain small exposure and favor more conservatively financed alternatives.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	6556	8190	16964	48335	55691	36096	31792	40523	54087	54213
Gross Profit	2454	3021	3876	5755	7277	7428	8099	9557	12429	14486
Gross Margin	37.4%	36.9%	22.8%	11.9%	13.1%	20.6%	25.5%	23.6%	23.0%	26.7%
SG&A Exp.	233	253	527	533	611	548	656	599	702	694
D&A Exp.	406	586								
Operating Profit	1044	1237	1360	2072	2840	2626	2891	3760	5779	7351
Operating Margin	15.9%	15.1%	8.0%	4.3%	5.1%	7.3%	9.1%	9.3%	10.7%	13.6%
Net Profit	193	310	304	196	633	1189	995	954	1694	3592
Net Margin	2.9%	3.8%	1.8%	0.4%	1.1%	3.3%	3.1%	2.4%	3.1%	6.6%
Free Cash Flow	(422)	(432)	(2193)	(1086)	(2206)	(6094)	(4449)	(4015)	99	2043
Income Tax	14	17	54	93	357	(123)	(258)	(1833)	4	195

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	17379	20897	48904	50330	64279	71189	78925	86246	88246	98880
Cash & Equivalents	86	126	372	590	847	606	467	336	419	291
Acc. Receivable	689	680	3057	3658	3378	2400	3557	4504	4009	5038
Inventories	366	328	1522	1807	1467	1636	2055	2022	1677	1935
Goodwill & Int. Ass.	2861	3111	8725	8158	13447	12904	11182	10884	10885	11321
Total Liabilities	11131	13509	32554	34051	41965	47591	56494	56266	57396	65035
Accounts Payable	449	512	3107	3834	3349	2274	3502	4685	3493	4118
Long-Term Debt	9381	11371	22053	23199	30485	36968	44052	44084	46028	51054
Total Equity	121	53	2113	1078	664	(932)	(1694)	(1196)	20559	21827

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	1.3%	1.6%	0.9%	0.4%	1.1%	1.8%	1.3%	1.2%	1.9%	3.8%
Return on Equity	319.5%	357.0%	28.1%	12.3%	72.7%				17.5%	16.9%
Shares Out.	892	892	1,120	1,123	1,081	1,047	1,047	1,079	2,619	2,650
Revenue/Share	7.35	9.18	15.90	43.09	51.06	33.91	29.48	35.21	37.01	20.55
FCF/Share	(0.47)	(0.48)	(2.06)	(0.97)	(2.02)	(5.73)	(4.12)	(3.49)	0.07	0.77

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