Tenaris SA (TS)

Updated December 6th, 2020 by Josh Arnold

Key Metrics

Current Price:	$17	**5 Year CAGR Estimate:**	1.7%	**Market Cap:**	$9.9 B
Fair Value Price:	$13	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	05/19/21[1]
% Fair Value:	133%	**5 Year Valuation Multiple Estimate:**	-5.6%	**Dividend Payment Date:**	05/30/21[2]
Dividend Yield:	1.6%	**5 Year Price Target**	$17	**Years Of Dividend Growth:**	N/A
Dividend Risk Score:	F	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	N/A

Overview & Current Events

Tenaris SA is a global manufacturer of steel pipes and related services that is headquartered in Luxembourg and is a majority-owned subsidiary of the Techint Group. Tenaris has significant exposure to oil prices as the majority of its customers operate in the energy sector. Its common stock is traded on three international stock exchanges, but U.S. investors can initiate a stake in the business through ADR shares. The company produces about $5 billion in annual revenue under normal conditions and currently has a market capitalization of $9.9 billion.

Tenaris reported third quarter earnings on November 4th, 2020 with results coming in better than expected on both the top and bottom lines. Revenue in Q3 was down -18% quarter-over-quarter and down -43% year-over-year, but the company's total of $1 billion in revenue was meaningfully better than expectations.

Drilling activity declined further in the quarter as oil prices have remained low, impacting the company's top line. Selling prices also declined during the quarter, creating another revenue headwind.

EBITDA was $107 million, down -66% year-over-year, but nearly doubled from the trough set in this year's Q2 as the company concentrated efforts on cost reductions. Free cash flow was $376 million, and net cash was $1.1 billion at the end of the quarter. The company used this strong free cash flow to reinstate its dividend, which was $0.14 per share for the half-year, as Tenaris typically pays two dividends per year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$1.90	$2.26	$2.88	$2.62	$2.28	$1.08	$0.15	$0.77	$1.48	$1.26	***-$0.15***	***$1.00***
DPS	$0.68	$0.68	$0.76	$0.86	$0.90	$0.90	$0.90	$0.82	$0.82	$0.82	***$0.28***	***$0.28***
Shares[3]	590	590	590	590	590	590	590	590	590	590	***590***	***590***

Tenaris' growth over the last decade has been far from constant, but this is largely due to the prolonged downturn in oil prices that began in 2014. Since the majority of Tenaris' customers operate within the energy sector, this reduces demand for its products and services and causes a decline in its aggregate sales.

Last year saw a strong rebound in Tenaris' earnings capacity. However, oil prices remain a key risk for Tenaris; much lower oil and gas prices have significantly impaired the company's ability to produce earnings in 2020. Tenaris is beholden to capital expenditures of oil and gas producers, which generally decline when oil prices remain low for long periods of time, as we're seeing now. Our estimate of intermediate-term growth is 6%. Should coronavirus fears be prolonged, oil prices would almost certainly suffer, and with that, Tenaris' earnings. While Q3 results showed improvement in many ways, Tenaris is still a long way from normalized conditions. Given this, we use an earnings power estimate of $0.75 per share for our valuation and fair value calculations.

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[1] Estimated date
[2] Estimated date
[3] Share count in millions

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	21.6	18.1	13.3	16.6	18.5	25.2	---	40.3	22.6	19.3	***22.7***	***17.0***
Avg. Yld.	1.7%	1.7%	2.0%	2.0%	2.1%	3.3%	3.4%	2.6%	2.5%	3.4%	***1.6%***	***1.6%***

Tenaris has traded at an average price-to-earnings ratio (P/E) of 17 over the last decade, if we exclude the years in which its P/E ratio was artificially elevated due to depressed earnings caused by the decline in oil prices. We use 17 times earnings power as our estimate of fair value given that Tenaris appears to be on the way to recovery. Today, shares trade for 22.7 times our earnings power estimate, which means we expect a sizable negative impact from the valuation if the multiple were to revert to our fair value P/E estimate of 17 over time. Shares have nearly doubled in the six weeks leading up to this update, so the valuation has deteriorated enormously.

For income investors, we note that the country of Luxembourg imposes a 15% withholding tax on Tenaris' dividend payments. We expect the payout to rise back to ~30% of earnings by 2025, or $0.28 at current estimates. This is consistent with the company's dividend posture coming out of the Great Recession.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	36%	30%	26%	33%	40%	83%	600%	107%	55%	65%	***37%***	***28%***

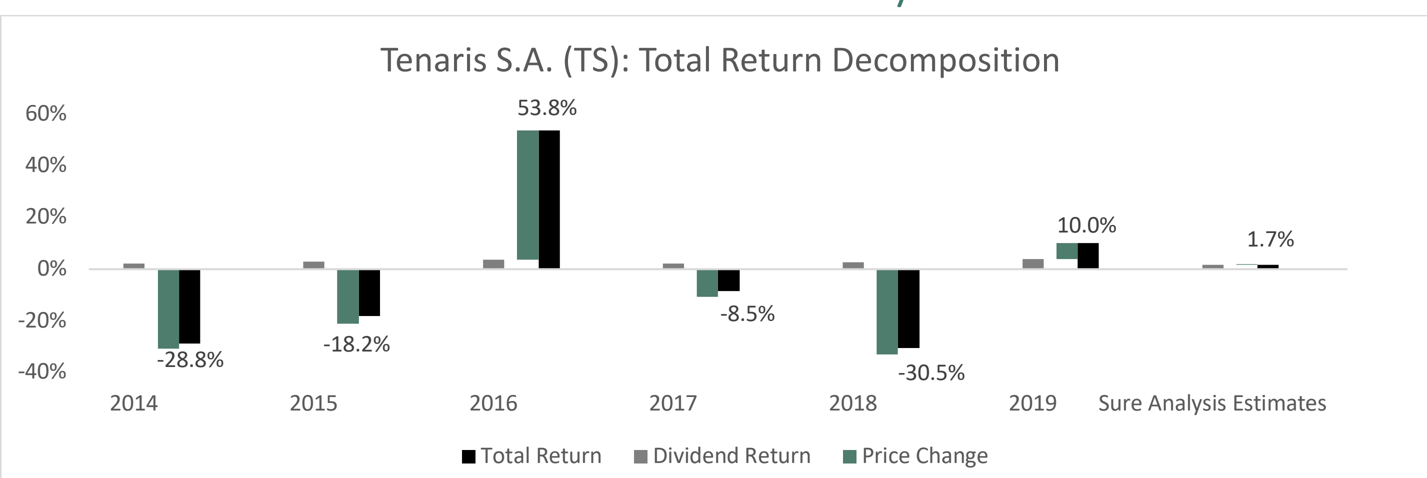
Tenaris has reinstated its payout, albeit at a relatively low level. We see the dividend outlook as murky at the moment but look for greater clarity in the next couple of quarters.

Qualitatively, Tenaris' most compelling competitive advantage is its entrenched position in a technical segment of the energy sector that relies tremendously on strong customer-supplier relationships. As a large company with global operations, Tenaris' services are unlikely to be replaced by newer, smaller industry disruptors. Its leverage to the oil and gas markets has been both a blessing and a curse in recent quarters. Tenaris is not susceptible to recessions so much as oil prices, so investors should focus on the latter, not the former, when assessing safety.

Final Thoughts & Recommendation

We see Tenaris as having the pieces in place to continue to recover, but we also see the massive rally in the stock as being overdone. With total returns of just 1.7% projected for the next five years, we rate Tenaris a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	7712	9972	10834	10597	10141	6903	4294	5289	7659	7294
Gross Profit	2963	3699	4197	4140	4001	2155	1128	1603	2379	2187
Gross Margin	38.4%	37.1%	38.7%	39.1%	39.5%	31.2%	26.3%	30.3%	31.1%	30.0%
SG&A Exp.	1170	1431	1412	1483	1478	1151	853	994	1190	1167
D&A Exp.	507	554	568	610	616	659	662	609	664	540
Operating Profit	1449	1842	2354	2181	2083	560	-64	330	867	827
Op. Margin	18.8%	18.5%	21.7%	20.6%	20.5%	8.1%	-1.5%	6.2%	11.3%	11.3%
Net Profit	1127	1332	1699	1551	1159	-80	55	545	876	743
Net Margin	14.6%	13.4%	15.7%	14.6%	11.4%	-1.2%	1.3%	10.3%	11.4%	10.2%
Free Cash Flow	33	427	1074	1635	902	1094	100	-575	267	1180
Income Tax	396	475	542	628	580	234	17	-17	229	202

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	14364	14864	15960	15931	16511	14887	14003	14398	14251	14843
Cash & Equivalents	844	824	828	615	418	287	400	330	428	1554
Acc. Receivable	1422	1912	2077	2005	2003	1216	1026	1241	1779	1348
Inventories	2460	2806	2986	2703	2780	1843	1564	2368	2524	2266
Goodwill & Int.	3582	3376	3200	3067	2758	2143	1863	1661	1466	1562
Total Liabilities	3814	3691	4460	3461	3704	3021	2590	2817	2376	2657
Accounts Payable	818	902	883	835	832	504	557	751	694	556
Long-Term Debt	1244	931	1742	929	998	971	840	966	539	822
Total Equity	9902	10506	11328	12290	12654	11713	11287	11482	11783	11989
D/E Ratio	0.13	0.09	0.15	0.08	0.08	0.08	0.07	0.08	0.05	0.07

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	8.1%	9.1%	11.0%	9.7%	7.1%	-0.5%	0.4%	3.8%	6.1%	5.1%
Return on Equity	11.9%	13.0%	15.6%	13.1%	9.3%	-0.7%	0.5%	4.8%	7.5%	6.2%
ROIC	9.8%	11.1%	13.4%	11.6%	8.5%	-0.6%	0.4%	4.4%	7.0%	5.8%
Shares Out.	590	590	590	590	590	590	590	590	590	590
Revenue/Share	13.06	16.89	18.35	17.95	17.18	11.69	7.27	8.96	12.97	12.36
FCF/Share	0.06	0.72	1.82	2.77	1.53	1.85	0.17	-0.97	0.45	2.00

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