



National Fuel Gas Co. (NFG)

Updated February 5th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	\$41	5 Year CAGR Estimate:	12.1%	Market Cap:	\$3.7 B
Fair Value Price:	\$57	5 Year Growth Estimate:	2.0%	Ex-Dividend Date:	3/29/2021 ¹
% Fair Value:	72%	5 Year Valuation Multiple Estimate:	6.8%	Dividend Payment Date:	4/14/2021 ¹
Dividend Yield:	4.4%	5 Year Price Target	\$63	Years Of Dividend Growth:	50
Dividend Risk Score:	A	Retirement Suitability Score:	A	Last Dividend Increase:	2.3%

Overview & Current Events

National Fuel Gas Co. is a diversified energy company that operates in five business segments: Exploration & Production, Pipeline & Storage, Gathering, Utility, and Energy Marketing. The company's largest segment is Exploration & Production. National Fuel Gas was founded in 1902 and has grown to a market capitalization of \$3.7 billion. With 50 years of consecutive dividend increases, National Fuel Gas qualifies to be a Dividend Champion.

In early February, National Fuel Gas reported (2/4/21) financial results for the first quarter of fiscal 2021. The company grew its production by an impressive 36% over the prior year's quarter, primarily thanks to the acquisition of Appalachian assets. The average price of natural gas fell -8%, from \$2.32 in the prior year's quarter to \$2.14, after the effect of hedging. Nevertheless, the increased volumes resulted in a 5% increase in the adjusted earnings-per-share, from \$1.01 to \$1.06.

National Fuel Gas is facing a headwind due to the coronavirus crisis, but the pandemic has affected the natural gas market much less than the oil market. In addition, the pipeline & storage and gathering segments provide a strong buffer to earnings amid low commodity prices. Both segments grew their EBITDA 35% in the latest quarter thanks to strong volume growth. Management expects strong production growth in fiscal 2021 and raised its guidance for a second consecutive quarter thanks to higher expected prices and lower production costs. It now expects earnings-per-share of \$3.65-\$3.95 (vs. previous guidance of \$3.55-\$3.85), for 30% growth at the mid-point. We expect record earnings-per-share of \$3.80 in this fiscal year.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$3.09	\$2.63	\$3.14	\$3.52	-\$4.50	-\$3.43	\$3.30	\$3.34	\$3.45	\$2.92	\$3.80	\$4.20
DPS	\$1.40	\$1.44	\$1.48	\$1.52	\$1.56	\$1.60	\$1.64	\$1.68	\$1.72	\$1.76	\$1.80	\$2.00
Shares²	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0	86.8	91.0	91.5	94.0

National Fuel Gas pursues growth by growing its natural gas production and expanding its pipeline network. However, the company's earnings have barely grown over the last decade. Earnings-per-share have compounded at a rate of 2.9% per year since 2010. Moreover, the pandemic has somewhat hurt natural gas prices in recent quarters but the strong production growth of National Fuel Gas will more than offset this headwind this year. Due to the high comparison base formed by the all-time high earnings expected in this fiscal year, we are forecasting 2% long-term earnings-per-share growth for this Dividend Champion, which allows us to calculate a 2026 earnings-per-share estimate of \$4.20.

Investors should note that 90% of the production of National Fuel Gas is natural gas. Therefore, as the Exploration & Production segment generates about half of total profits, the earnings of the company greatly depend on the price of natural gas. As a result, there is always great uncertainty in the long-term forecasts of the earnings of this company. This is the main reason behind our conservative growth forecast.

¹ Estimated date.

² In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	21.4	19.3	18.6	20.6	---	---	17.2	12.8	15.6	14.6	10.8	15.0
Avg. Yld.	2.8%	2.1%	2.8%	2.5%	2.1%	2.5%	3.1%	2.9%	3.2%	4.1%	4.4%	3.2%

National Fuel Gas is trading at a price-to-earnings ratio of 10.8, which is much lower than its historical 10-year average of 17.5. As we expect record earnings by 2026, we assume a fair price-to-earnings ratio of 15.0 for that year. If the stock reverts to this valuation level over the next 5 years, it will enjoy a 6.8% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2020	2026
Payout	45.3%	54.8%	47.1%	43.2%	---	---	49.7%	50.3%	50.0%	60.3%	47.4%	47.6%

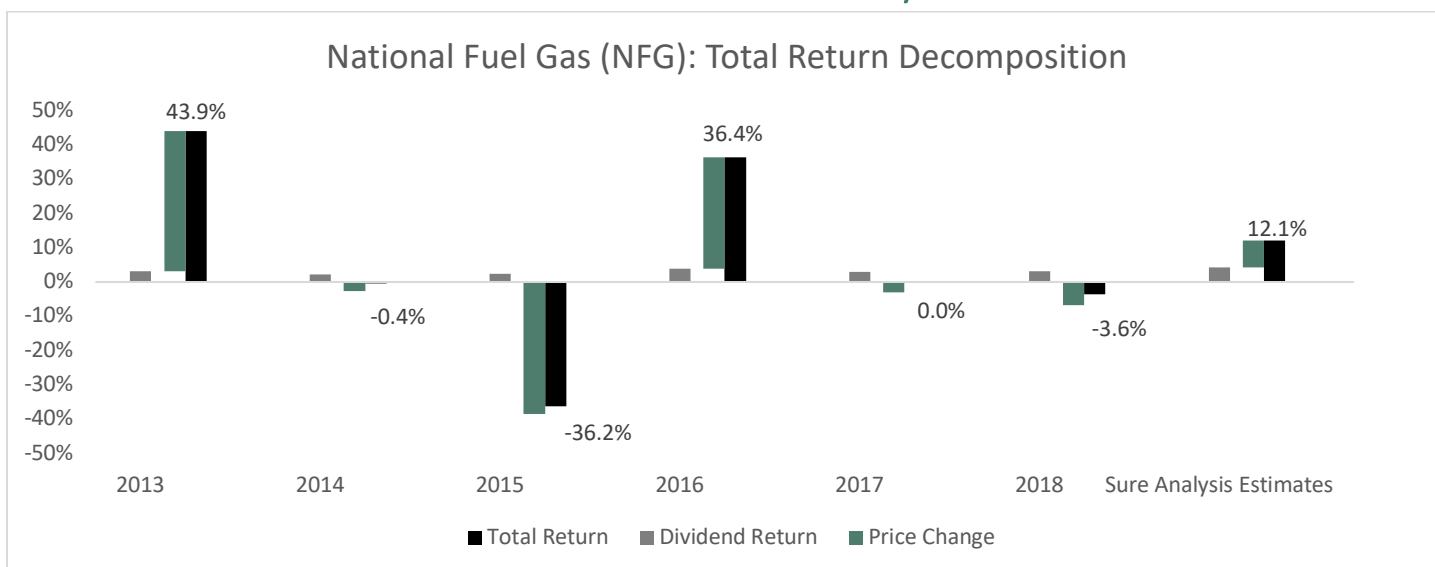
National Fuel Gas has a healthy balance sheet while its interest coverage level stands at a decent level, around 4.0. Moreover, its dividend payout ratio is sufficiently low to enable continued dividend growth even if earnings stall temporarily. Management has always targeted a dividend payout ratio around 50% in order to have a high margin of safety against the wide fluctuations of the price of natural gas. As the 4.4% dividend yield of National Fuel Gas is nearly triple the yield of the S&P (1.5%), the stock may entice income-oriented investors. However, these investors should be aware of the company's high dependence on the price of natural gas.

Qualitatively, National Fuel Gas' competitive advantage is its combination of regulated and stable businesses (like pipelines and utilities) with cyclical and potentially higher-growth sectors (like exploration & production). This allows the company to endure difficult operating environments and downturns, such as the ongoing one, with less difficulty than its peers who may focus exclusively on the more cyclical areas of the energy sector.

Final Thoughts & Recommendation

Thanks to its sustained production growth, its promising outlook and its reasonable valuation, National Fuel Gas could offer a 12.1% average annual return over the next five years. This stems from 2% growth, a 4.4% starting yield and a potential valuation tailwind. Shares earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	1,779	1,627	1,830	2,113	1,761	1,452	1,580	1,593	1,693	1,546
Gross Profit	924	940	1,042	1,123	1,075	1,055	1,080	1,014	1,031	568
Gross Margin	51.9%	57.8%	57.0%	53.2%	61.0%	72.6%	68.4%	63.7%	60.9%	36.7%
Operating Profit	441	448	518	570	515	532	594	520	512	479
Operating Margin	24.8%	27.5%	28.3%	27.0%	29.3%	36.6%	37.6%	32.6%	30.2%	31.0%
Net Profit	258	220	260	299	(379)	(291)	283	392	304	(124)
Net Margin	14.5%	13.5%	14.2%	14.2%	-21.5%	-20.0%	17.9%	24.6%	18.0%	-8.0%
Free Cash Flow	(160)	(376)	35	(5)	(165)	7	234	31	(94)	(482)
Income Tax	164	151	173	190	(319)	(233)	161	(7)	85	19

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	5,221	5,935	6,218	6,728	6,565	5,636	6,103	6,036	6,462	6,965
Cash & Equivalents	80	74	65	37	114	130	556	230	20	21
Accounts Receivable	163	116	133	150	105	133	112	141	140	144
Inventories	82	78	94	67	65	71	74	78	80	85
Goodwill & Int. Ass.	5	5	5	5	5	5	5	5	5	5
Total Liabilities	3,329	3,975	4,024	4,317	4,539	4,109	4,400	4,099	4,323	4,993
Accounts Payable	142	88	105	137	180	108	126	160	132	134
Long-Term Debt	1,089	1,570	1,649	1,723	2,084	2,086	2,384	2,131	2,189	2,660
Shareholder's Equity	1,892	1,960	2,195	2,411	2,025	1,527	1,704	1,937	2,139	1,972
D/E Ratio	0.58	0.80	0.75	0.71	1.03	1.37	1.40	1.10	1.02	1.35

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	5.0%	3.9%	4.3%	4.6%	-5.7%	-4.8%	4.8%	6.5%	4.9%	-1.8%
Return on Equity	14.2%	11.4%	12.5%	13.0%	-17.1%	-16.4%	17.5%	21.5%	14.9%	-6.0%
ROIC	8.6%	6.8%	7.1%	7.5%	-9.2%	-7.5%	7.4%	9.6%	7.2%	-2.8%
Shares Out.	82.9	83.3	83.7	84.2	84.6	85.1	85.5	86.0	86.8	88.0
Revenue/Share	21.26	19.43	21.69	24.87	20.87	17.12	18.37	18.43	19.51	17.58
FCF/Share	(1.92)	(4.49)	0.42	(0.06)	(1.95)	0.09	2.72	0.36	(1.09)	(5.47)

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

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