



# Pembina Pipeline Corp. (PBA)

Updated March 5<sup>th</sup>, 2021 by Aristofanis Papadatos

## Key Metrics

|                             |      |  |       |                                  |          |
|-----------------------------|------|--|-------|----------------------------------|----------|
| <b>Current Price:</b>       | \$28 | <b>5 Year CAGR Estimate:</b>               | 6.9%  | <b>Market Cap:</b>               | \$14.6 B |
| <b>Fair Value Price:</b>    | \$24 | <b>5 Year Growth Estimate:</b>             | 4.0%  | <b>Ex-Dividend Date:</b>         | 2/24/21  |
| <b>% Fair Value:</b>        | 117% | <b>5 Year Valuation Multiple Estimate:</b> | -3.0% | <b>Dividend Payment Date:</b>    | 3/15/21  |
| <b>Dividend Yield:</b>      | 7.0% | <b>5 Year Price Target</b>                 | \$29  | <b>Years Of Dividend Growth:</b> | 5        |
| <b>Dividend Risk Score:</b> | F    | <b>Retirement Suitability Score:</b>       | D     | <b>Last Dividend Increase:</b>   | 5.0%     |

## Overview & Current Events

Pembina Pipeline Corporation is based in Calgary, Canada. It has been serving the energy industry of North America with its transportation and midstream services for 65 years. It owns an integrated system of pipelines that transport various hydrocarbon liquids and natural gas products produced primarily in western Canada. The company also has gathering and processing facilities. Pembina has a market cap of \$14.6 billion and operates in three segments: Pipelines, Facilities, and Marketing & New Ventures. In 2020, these segments generated 57%, 30% and 13% of the company's total gross profit, respectively. All the figures in this report are in US dollars.

In late February, Pembina reported (2/25/21) financial results for the fourth quarter of fiscal 2020. In the year, the assets acquired from Kinder Morgan helped mitigate the impact of the pandemic but the suppressed prices of oil and NGL caused lower producer activity and a decline in transported volumes. In addition, the marketing segment was hurt by lower margins in crude oil and NGL. As a result, earnings-per-share decreased -16% over the prior year.

Pembina is facing a headwind from the pandemic, which has caused a severe downturn in the energy market. This downturn has caught Pembina off guard, with a material debt load. As a result, Pembina cut its capital expenses by -37% last year and deferred some growth projects. On the bright side, the pandemic could subside in the second half of this year thanks to the ongoing vaccination program. As a result, we expect Pembina to earn \$2.00 per share this year.

## Growth on a Per-Share Basis

| Year                      | 2011   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   | 2021          | 2026          |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| <b>EPS</b>                | \$1.00 | \$0.87 | \$1.09 | \$0.92 | \$0.77 | \$0.73 | \$1.43 | \$1.76 | \$2.00 | \$1.68 | <b>\$2.00</b> | <b>\$2.43</b> |
| <b>DPS</b>                | \$1.58 | \$1.60 | \$1.60 | \$1.50 | \$1.35 | \$1.38 | \$1.57 | \$1.73 | \$1.78 | \$1.87 | <b>\$1.97</b> | <b>\$2.00</b> |
| <b>Shares<sup>1</sup></b> | 168    | 259    | 308    | 328    | 348    | 389    | 432    | 509    | 518    | 550    | <b>550</b>    | <b>700</b>    |

During the last decade, although Pembina has more than tripled its share count, it has grown its earnings-per-share at a 5.9% average annual rate. This growth has not been uniform, as the company failed to grow its earnings-per-share from 2010 to 2016. Nevertheless, the company has a long backlog of additional growth projects. Thanks to these projects, management previously stated that it expected to grow adjusted cash flow per share by 8%-10% per year and raise the dividend by about 5% per year beyond this year. Due to the volatile record of Pembina, we prefer to be somewhat conservative and thus we expect the company to grow its earnings-per-share by 4% per year beyond this year.

## Valuation Analysis

| Year             | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Now         | 2026        |
|------------------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| <b>Avg. P/E</b>  | 32.9 | 41.7 | 36.5 | 48.3 | 37.4 | 36.4 | 23.1 | 19.2 | 18.2 | 15.5 | <b>14.0</b> | <b>12.0</b> |
| <b>Avg. Yld.</b> | 4.8% | 4.4% | 4.0% | 3.4% | 4.7% | 5.2% | 4.8% | 5.1% | 4.9% | 7.2% | <b>7.0%</b> | <b>6.8%</b> |

Pembina has traded at remarkably high price-to-earnings ratios through much of the last decade. In addition, due to its huge capital expenses on growth projects, the company has posted negative free cash flows in most years so we cannot

<sup>1</sup> In millions.

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use cash flows to evaluate the stock. The stock is now trading at a price-to-earnings ratio of 14.0, which is higher than our assumed fair earnings multiple of 12.0. We have assumed such a low fair earnings multiple due to the appreciable debt load of the company. If the stock trades at our fair value estimate in five years, it will incur a -3.0% annualized drag in its returns.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

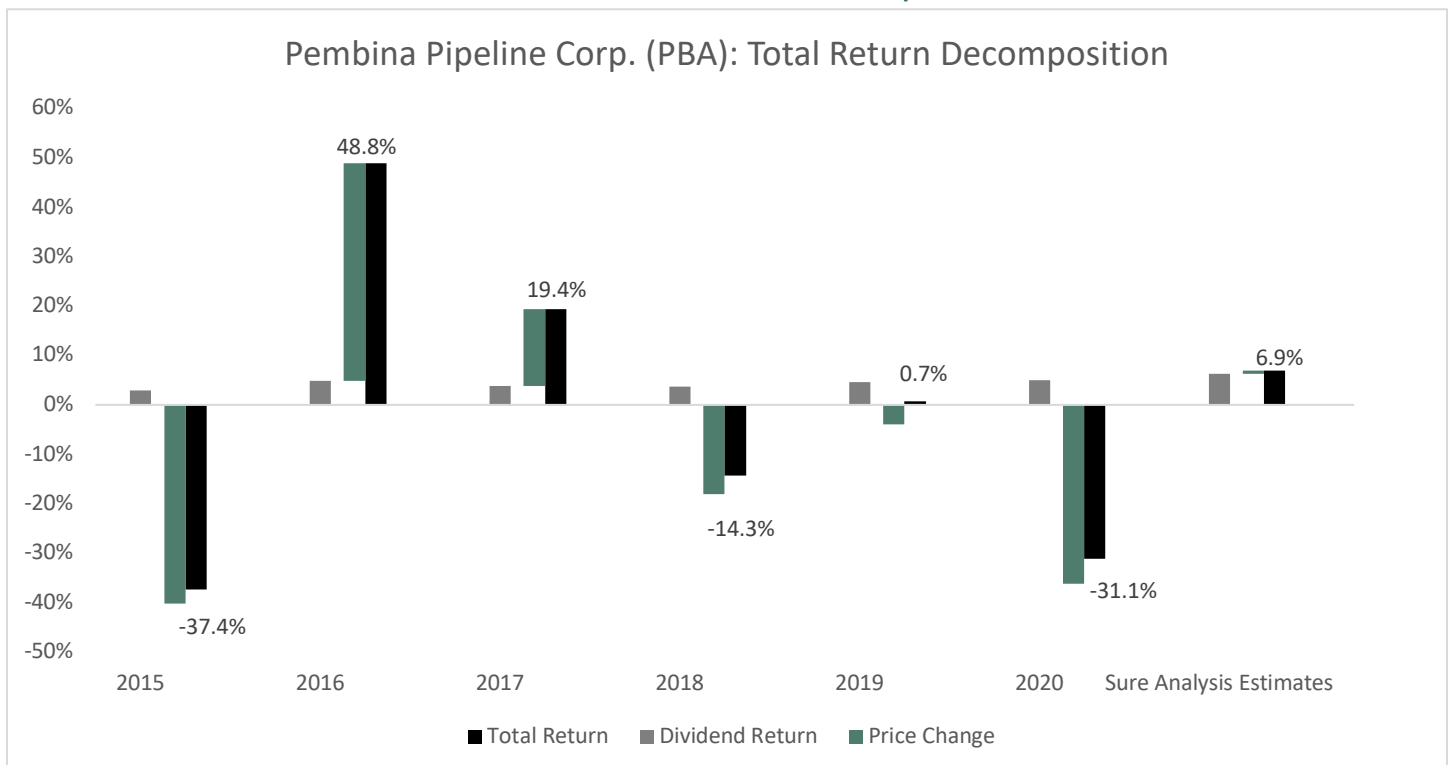
| Year   | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018  | 2019  | 2020 | 2021         | 2026         |
|--------|------|------|------|------|------|------|------|-------|-------|------|--------------|--------------|
| Payout | 158% | 184% | 147% | 162% | 176% | 188% | 110% | 98.2% | 89.1% | 111% | <b>98.5%</b> | <b>82.2%</b> |

The competitive advantage of Pembina lies in its large scale and its integrated assets in some of the most prolific resource plays in North America. Pembina has steadily increased the fee-based portion of its EBITDA, from 77% in 2015 to 90%-95% this year. It has pursued this strategy in order to secure a reliable and growing dividend, which is the top priority of management. Pembina has raised its dividend (in CAD) for 8 consecutive years and pays dividends on a monthly basis, which is enticing for income-oriented investors. In addition, it has a stronger balance sheet than most midstream companies, with its credit rating standing at a BBB level. However, the company has been caught in the ongoing downturn with a significant debt load, with its current liabilities of \$1.4 billion (due in the next 12 months) exceeding its current assets of \$0.8 billion. If the pandemic lasts longer than expected, investors should be aware that the dividend may come under pressure due to the elevated payout ratio and the significant debt load of the company.

## Final Thoughts & Recommendation

Pembina could recover strongly from the pandemic in the second half of the year, but the market has already priced part of the recovery in the stock. As a result, we expect the stock to offer a 6.9% average annual return over the next five years. We thus rate the stock as a hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

| Year                    | 2011  | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  | 2020  |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Revenue</b>          | 1,695 | 3,428 | 4,861 | 5,497 | 3,632 | 3,221 | 4,167 | 5,672 | 5,447 | 4,629 |
| <b>Gross Profit</b>     | 348   | 507   | 764   | 772   | 652   | 809   | 1,103 | 1,462 | 1,840 | 1,499 |
| <b>Gross Margin</b>     | 20.5% | 14.8% | 15.7% | 14.0% | 18.0% | 25.1% | 26.5% | 25.8% | 33.8% | 32.4% |
| <b>SG&amp;A Exp.</b>    | 63    | 97    | 128   | 141   | 123   | 147   | 182   | 215   | 223   | 184   |
| <b>D&amp;A Exp.</b>     | 71    | 180   | 166   | 205   | 206   | 221   | 295   | 322   | 382   | 522   |
| <b>Operating Profit</b> | 285   | 410   | 635   | 614   | 510   | 663   | 899   | 1,225 | 1,606 | 1,329 |
| <b>Op Margin</b>        | 16.8% | 12.0% | 13.1% | 11.2% | 14.0% | 20.6% | 21.6% | 21.6% | 29.5% | 28.7% |
| <b>Net Profit</b>       | 168   | 225   | 341   | 347   | 318   | 352   | 681   | 986   | 1,135 | (236) |
| <b>Net Margin</b>       | 9.9%  | 6.6%  | 7.0%  | 6.3%  | 8.8%  | 10.9% | 16.4% | 17.4% | 20.8% | -5.1% |
| <b>Free Cash Flow</b>   | (194) | (224) | (189) | (554) | (791) | (504) | (252) | 795   | 668   | 913   |

## Balance Sheet Metrics

| Year                            | 2011  | 2012  | 2013  | 2014  | 2015  | 2016   | 2017   | 2018   | 2019   | 2020   |
|---------------------------------|-------|-------|-------|-------|-------|--------|--------|--------|--------|--------|
| <b>Total Assets</b>             | 3,271 | 8,327 | 8,586 | 9,701 | 9,297 | 11,138 | 20,331 | 19,685 | 25,075 | 24,637 |
| <b>Cash &amp; Equivalents</b>   | ---   | 27    | 48    | 46    | 20    | 26     | 255    | 115    | 99     | 64     |
| <b>Accounts Receivable</b>      | 143   | 326   | 394   | 364   | 331   | 119    | 141    | 444    | 440    | 453    |
| <b>Inventories</b>              | 21    | 109   | 149   | 118   | 86    | 134    | 134    | 145    | 96     | 173    |
| <b>Goodwill &amp; Int. Ass.</b> | 239   | 2,637 | 2,408 | 2,447 | 2,034 | 2,102  | 3,749  | 3,237  | 4,933  | 4,972  |
| <b>Total Liabilities</b>        | 2,329 | 4,030 | 3,729 | 4,243 | 3,948 | 4,985  | 9,324  | 9,032  | 12,162 | 12,862 |
| <b>Accounts Payable</b>         | 139   | 303   | 337   | 382   | 269   | 352    | 370    | 584    | 549    | 340    |
| <b>Long-Term Debt</b>           | 1,593 | 2,568 | 2,137 | 2,465 | 2,395 | 3,079  | 6,009  | 5,520  | 7,772  | 8,529  |
| <b>Shareholder's Equity</b>     | 942   | 4,292 | 4,485 | 4,700 | 4,557 | 5,034  | 9,031  | 8,829  | 10,604 | 9,418  |
| <b>D/E Ratio</b>                | 1.69  | 0.60  | 0.44  | 0.45  | 0.45  | 0.50   | 0.55   | 0.52   | 0.60   | 0.73   |

## Profitability & Per Share Metrics

| Year                    | 2011  | 2012  | 2013  | 2014  | 2015  | 2016 | 2017 | 2018  | 2019  | 2020  |
|-------------------------|-------|-------|-------|-------|-------|------|------|-------|-------|-------|
| <b>Return on Assets</b> | 5.5%  | 3.9%  | 4.0%  | 3.8%  | 3.3%  | 3.4% | 4.3% | 4.9%  | 5.1%  | -0.9% |
| <b>Return on Equity</b> | 16.8% | 8.6%  | 7.8%  | 7.6%  | 6.9%  | 7.3% | 9.7% | 11.0% | 11.7% | -2.4% |
| <b>ROIC</b>             | 6.8%  | 4.8%  | 4.9%  | 4.7%  | 4.1%  | 4.1% | 5.2% | 5.9%  | 6.2%  | -1.2% |
| <b>Shares Out.</b>      | 168   | 259   | 308   | 328   | 348   | 389  | 432  | 509   | 518   | 550   |
| <b>Revenue/Share</b>    | 10.08 | 13.21 | 15.78 | 16.76 | 10.44 | 8.28 | 9.65 | 11.14 | 10.60 | 8.42  |

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

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