Sempra Energy (SRE)

Updated May 17th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	$138	**5 Year CAGR Estimate:**	9.6%	**Market Cap:**	$41.8 B
Fair Value Price:	$151	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	6/24/2021[1]
% Fair Value:	91%	**5 Year Valuation Multiple Estimate:**	1.9%	**Dividend Payment Date:**	7/15/2021
Dividend Yield:	3.2%	**5 Year Price Target**	$193	**Years Of Dividend Growth:**	11
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	5.3%

Overview & Current Events

Sempra Energy (SRE) was founded 20 years ago and has grown into a $41.8 billion market cap company. It serves one of the largest utility customer bases in the U.S., as it distributes natural gas and electricity in Southern California (over 20 million customers) and owns a majority stake in Texas-based Oncor, a transmission and distribution business (over 10 million customers). The company also owns and operates other utilities and merchant renewable energy projects, liquefied natural gas facilities, and gas pipes and storage in the U.S. and Latin America.

Sempra Energy benefits from two key trends, namely the transition towards cleaner energy resources and the advance of the U.S. as a global energy leader. In 2018, the company sold most of its non-core assets in order to better focus on its large core North American regulated utility, LNG export, and Mexican infrastructure (IEnova) assets as well as deleverage the balance sheet. Given the strong competitive advantages enjoyed by these core assets, we believe that these moves have made Sempra Energy more attractive.

On April 5th, 2021, Sempra Energy agreed to sell a non-controlling, 20% interest in Sempra Infrastructure to KKR for $3.37 billion in cash. The company will use the proceeds to fund its growth projects.

In early May, Sempra Energy reported (5/5/21) financial results for the first quarter of fiscal 2021. Adjusted earnings-per-share grew 19%, from $2.47 to $2.95, primarily thanks to high growth in the earnings of Cameron LNG and strong performance in the regulated business in California. As a utility, Sempra Energy is essentially immune to the pandemic. It raised the dividend by 5.3% this year and reaffirmed its guidance for earnings-per-share of $7.50-$8.10 in 2021. We view this guidance as somewhat conservative. Given also the fact that Sempra Energy has exceeded analysts' earnings-per-share estimates in 9 of the last 11 quarters, we expect it to earn approximately $8.05 per share this year.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$5.51	$3.48	$4.01	$4.63	$5.37	$5.46	$5.42	$5.57	$6.78	$8.03	***$8.05***	***$10.27***
DPS	$1.92	$2.40	$2.52	$2.64	$2.80	$3.02	$3.29	$3.58	$3.87	$4.18	***$4.40***	***$5.62***
Shares[2]	242	247	249	251	251	251	252	270	289	290	***292***	***350***

Sempra's enormous economies of scale and regulated monopolies in California and Texas should enable it to capitalize on any economic growth in those regions to drive long term growth. Sempra Energy has a 5-year capital plan of $32 billion, which will be a growth driver in the upcoming years. Additionally, Sempra's assets in Mexico enjoy a first mover advantage, which should enable them to grow rapidly as Mexico begins to invest more seriously in its massively underdeveloped infrastructure. The LNG export portfolio should also see strong demand in the long run, as the U.S. continues its transition into a global energy exporting giant. As a result, management has several expansion projects, which should contribute significantly to the company's cash flows. As this year's expected record earnings will form a high base for future comparison, we expect 5% annual growth over the next five years.

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[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	10.1	20.7	22.3	24.1	17.3	18.5	19.8	19.4	19.8	16.1	***17.1***	***18.8***
Avg. Yld.	3.4%	3.3%	2.8%	2.4%	3.0%	3.0%	3.1%	3.3%	2.9%	3.2%	***3.2%***	***2.9%***

Sempra Energy is currently trading at a price-to-earnings ratio of 17.1, which is lower than its 10-year average of 18.8. We expect the stock to trade close to its average valuation level in five years. If this occurs, the stock will enjoy a 1.9% annualized expansion of its price-to-earnings ratio.

Safety, Quality, Competitive Advantage, & Recession Resiliency

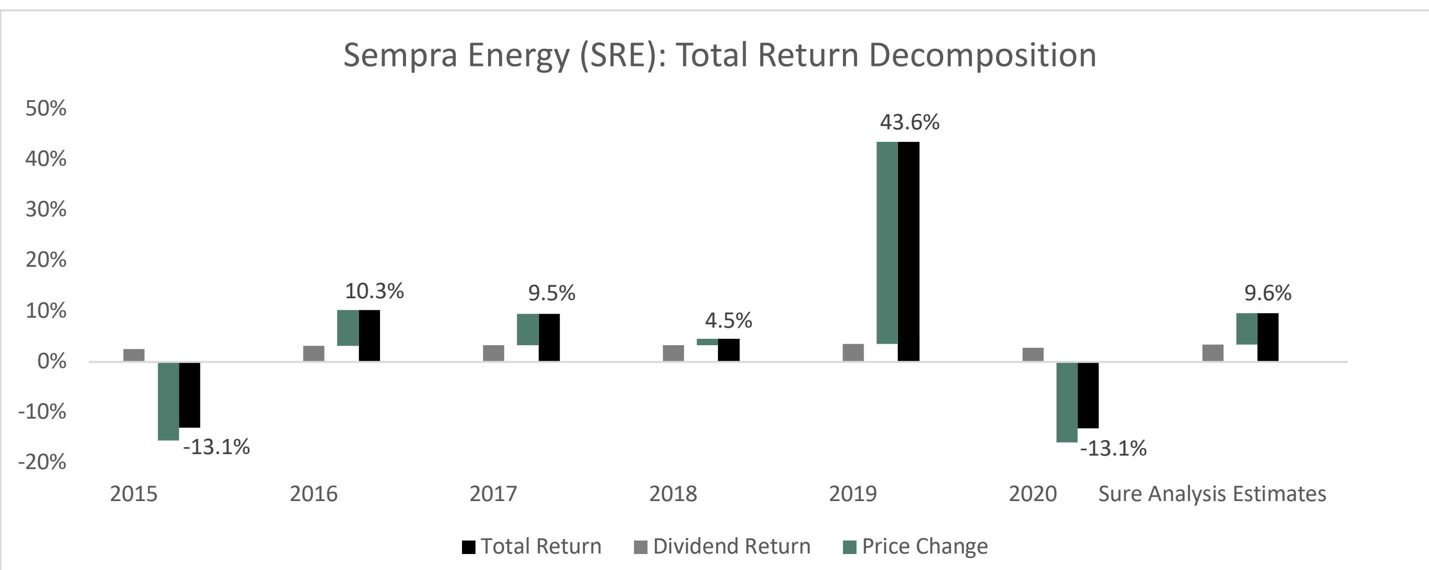
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	34.8%	69.0%	62.8%	57.0%	52.1%	55.3%	60.7%	64.3%	57.1%	52.1%	***54.7%***	***54.7%***

As a regulated utility in possession of dominant businesses in their respective regions, Sempra Energy possesses a clear moat around a significant portion of its earnings. At the same time, however, the regulated nature of its pricing prevents it from earning surplus profits. These businesses, as well as the stable, mission-critical nature of its infrastructure business in Mexico make it quite recession resistant. As proof of this, Sempra's earnings-per-share increased during the Great recession (2008 and 2009) and have increased in the ongoing recession as well. However, its LNG export business and international exposure make it susceptible to commodity price, geopolitical, and currency exchange risks. Nevertheless, its high-quality assets, low payout ratio, stable cash flows and strong growth prospects make it a fairly low-risk investment. Moreover, while the company has a somewhat weak balance sheet, it has improved its interest coverage ratio to 2.8 thanks to the sale of non-core assets.

Final Thoughts & Recommendation

Sempra Energy owns quality assets, many of which are in recession-resistant businesses. Its utilities businesses are dominant players in their fields and its LNG export and infrastructure businesses have strong growth prospects. Combined, they create a business that has both stable and defensive characteristics. The stock has rallied 17% in less than 3 months, but it can still offer a 9.6% average annual return over the next five years. It thus maintains its 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	10036	9647	10557	11035	10231	10183	11207	11687	10829	11370
Gross Profit	3065	3001	3371	3346	3592	3353	4277	4414	4692	5042
Gross Margin	30.5%	31.1%	31.9%	30.3%	35.1%	32.9%	38.2%	37.8%	43.3%	44.3%
D&A Exp.	976	1090	1113	1156	1250	1312	1490	1549	1569	1,666
Operating Profit	1845	1648	1959	1888	2026	1731	2519	2491	2627	2,833
Operating Margin	18.4%	17.1%	18.6%	17.1%	19.8%	17.0%	22.5%	21.3%	24.3%	24.9%
Net Profit	1339	865	1009	1162	1350	1371	257	1050	2198	3,933
Net Margin	13.3%	9.0%	9.6%	10.5%	13.2%	13.5%	2.3%	9.0%	20.3%	34.6%
Free Cash Flow	-977	-938	-788	-962	-258	-1903	-324	-337	-620	-2,085
Income Tax	394	59	366	300	341	389	1276	96	315	249

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	33249	36499	37244	39651	41150	47786	50454	60638	65665	66,623
Cash & Equivalents	252	475	904	570	403	349	288	190	108	960
Acc. Receivable	1198	1146	1308	1242	1283	1390	1307	1488	1261	1,578
Inventories	346	408	287	396	298	258	307	296	277	308
Goodwill & Int.	1484	1547	1450	1346	1223	2912	2993	2645	1815	1,804
Total Liabilities	23071	25816	25394	27551	28571	32545	35314	41390	43860	41,689
Accounts Payable	983	976	1088	1198	1133	1346	1350	1324	1234	1,359
Long-Term Debt	10863	12892	12945	14288	14663	17121	19412	25363	25816	24,206
Total Equity	9795	10302	11028	11346	11829	12971	12690	14900	17691	20,246
D/E Ratio	1.11	1.25	1.17	1.26	1.24	1.32	1.53	1.48	1.29	1.03

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	4.2%	2.5%	2.7%	3.0%	3.3%	3.1%	0.5%	1.9%	3.5%	5.9%
Return on Equity	14.2%	8.6%	9.5%	10.4%	11.7%	11.1%	2.0%	7.6%	13.5%	20.7%
ROIC	6.7%	3.9%	4.2%	4.5%	5.0%	4.6%	0.8%	2.7%	4.8%	8.1%
Shares Out.	242	247	249	251	251	251	252	270	289	290
Revenue/Share	41.55	39.11	42.34	44.02	40.77	40.54	44.42	43.31	38.40	38.90
FCF/Share	-4.05	-3.80	-3.16	-3.84	-1.03	-7.58	-1.28	-1.25	-2.20	-7.13

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