



Alliance Resource Partners (ARLP)

Updated October 28th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$12.14	5 Year CAGR Estimate:	5.8%	Market Cap:	\$1.54B
Fair Value Price:	\$7.50	5 Year Growth Estimate:	8.0%	Ex-Dividend Date:	11/04/2021
% Fair Value:	162%	5 Year Valuation Multiple Estimate:	-9.2%	Dividend Payment Date:	11/12/2021
Dividend Yield:	6.6%	5 Year Price Target	\$11.02	Years Of Dividend Growth:	1
Dividend Risk Score:	D	Retirement Suitability Score:	D	Last Dividend Increase:	100%

Overview & Current Events

Alliance Resource Partners is the first publicly traded master limited partnership and the second-largest coal producer in the eastern United States. Apart from its primary operations of producing and marketing coal to major domestic and international utility users, the company also owns both mineral and royalty interests in premier oil & gas regions, like the Permian, Anadarko, and Williston Basins. Finally, the company provides terminal services, including the transportation and loading of coal and technology products and services. The company generates ~\$1.3 billion in annual revenues and is based in Tulsa, Oklahoma.

On October 25th, 2021, Alliance Resource Partners reported its Q3-2021 results for the quarter ended September 30th, 2021. Revenues grew by 16.8% year-over-year to \$415.4 million, significantly improving from Q3-2020. This was the result of higher coal sales volumes, which rose 10.3%, and significantly higher oil & gas prices. Further, EPU more than doubled at \$0.44, versus \$0.21 in the comparable period last year. EPU benefited from higher sales, ongoing cost control and efficiency initiatives at ARLP's mining operations, and reduced interest expenses due to the company's deleveraging strategy. Specifically, Alliance has now reduced its total debt and finance lease obligations by \$156.9 million year-to-date, improving its total leverage to a much more comfortable 0.95X (down from 1.08X in Q2.)

Management remains cautiously optimistic as its marketing team continues to add commitments to its coal contract book, entering into new agreements for the delivery of approximately 15.3 million tons over the balance of this year through 2024. Alliance is also likely to keep reducing its financial costs further. Combined with management's raised guidance for FY 2021, which now expects coal sales volume of 31.2M-32.6M tons (from 32.2M-33.6M previously), and with coal prices reaching record levels north of \$250 per metric ton amid a lack of global supply, we hike our EPU expectations for the year from \$1.00 to \$1.50. Following better than expected results, the company raised its quarterly distribution 100% to \$0.20.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPU¹	\$8.13	\$6.12	\$7.26	\$4.77	\$2.28	\$2.51	\$2.25	\$2.73	\$3.07	(\$1.02)	\$1.50	\$2.20
DPS	\$3.60	\$4.16	\$4.56	\$2.47	\$2.66	\$1.98	\$1.88	\$2.07	\$2.15	\$0.40	\$0.80	\$1.18
Units²	73.5	73.7	73.9	74	74.2	74.4	98.7	130.8	128.1	127.1	127.1	127.1

Alliance has been struggling over the past decade due to worldwide efforts to reduce the usage and production of coal in favor of renewable energy sources. The price of coal was slashed in half in 2020 from 2018. Since then, however, it has rebounded massively, hitting a 13-year high of \$269.5 per metric ton as of recently. Hence, while Alliance is facing significant regulation and media pushback, being one of the big remaining players in the industry, it is currently benefiting. We estimate EPU growth of 8% moving forward due to lower interest expenses, a better-than-expected recovery in the coal industry, and sky-high coal prices that were previously unexpected. We also expect distributions to grow at 8% annually as the company, following the improving trajectory of Alliance's profitability.

¹ Earnings Per limited Unit

² Units 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	4.3	4.9	5.1	8.8	13.0	4.0	9.5	7.6	6.5	---	8.1	5.0
Avg. Yld.	5.87%	5.12%	7.00%	5.92%	5.35%	20.0%	15.0%	9.40%	10.4%	12.6%	6.6%	10.7%

Alliance's valuation has been fluctuating to a broad range of multiples, following its volatile earnings and uncertainty regarding future operations. The stock's P/E based on our expected \$1.50 EPU for FY2021 points towards a valuation a bit higher than its historical average, which is likely due to investors expecting EPU growth in the medium term as the company gradually recovers from the pandemic. However, the company operates in one of the riskiest industries (coal) in a cyclical sector (fluctuating commodity prices). Hence, we believe that a fair P/E ratio is around 5.

Safety, Quality, Competitive Advantage, & Recession Resiliency

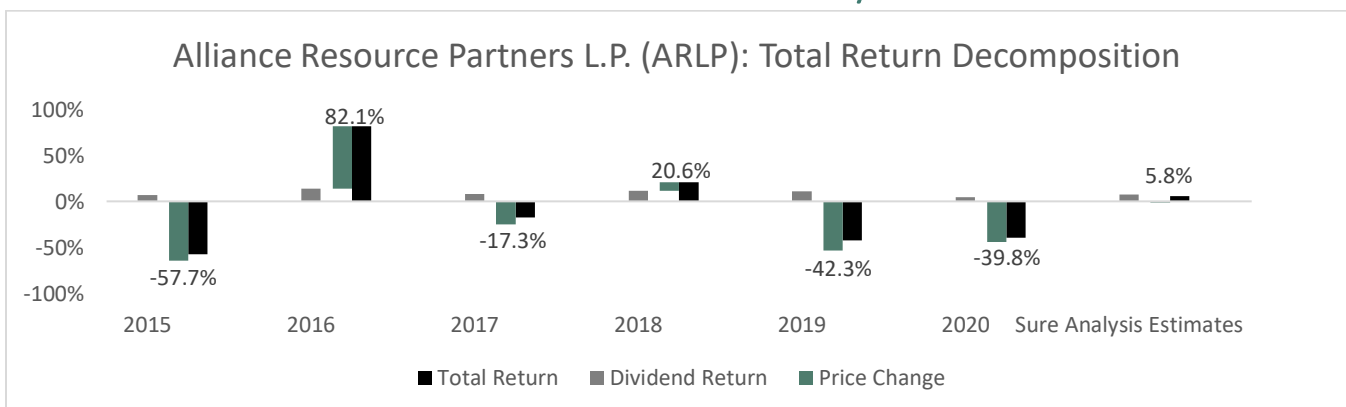
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	44%	68%	63%	52%	117%	79%	84%	76%	70%	---	53%	53%

Alliance's business model is seriously endangered from a combination of factors, including the "war" on combustible energy sources and reduced demand amid the pandemic's effects in industries such as the transportation sector, which still persist despite vaccinations rolling out successfully. The most recent quarter reflected the strengths of Alliance's position. By being one of the bigger remaining players in the coal market, Alliance benefits from the current supply shortage of coal, which raises commodity prices. Simultaneously, however, the fact that competitors are exiting the industry proves that it's not a favorable one moving forward. Considering that renewable energy sources continue replacing coal's demand, we believe that the company's long-term pathway remains uncertain. Alliance's investment case may end up being brighter if the sector stabilizes to a late-state of essentials-only coal demand. Until then, it's hard to trust ARLP and its distributions, despite the impressive distribution hike, and even though the company's financials could continue to positively progress in the medium term.

Final Thoughts & Recommendation

Alliance Resource Partners remains a highly volatile investment, operating in what the market rightfully sees as a much undesirable industry to be invested in. While the company may gradually grow its EPU and DPU in the medium term, it's hard to know its longevity prospects in the long run. We believe that even if the company enjoys growing EPU & DPU in the medium-term, the relatively hefty yield is still threatened by a potential valuation compression amid the company's operating field. We estimate annualized returns of around 5.8% through 2026. ARLP earns a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	2034	2206	2301	2274	1931	1796	2003	1962	1328
Gross Profit	1756	1906	2000	1916	1563	1486	1609	1530	447
Gross Margin	86.3%	86.4%	86.9%	84.3%	80.9%	82.7%	80.3%	78.0%	33.7%
SG&A Exp.	59	64	73	67	73	62	68	73	60
Operating Profit	394	444	544	462	368	332	333	275	129
Operating Margin	19.3%	20.1%	23.7%	20.3%	19.1%	18.5%	16.6%	14.0%	9.7%
Net Profit	336	393	497	306	339	304	367	399	-129
Net Margin	16.5%	17.8%	21.6%	13.5%	17.6%	16.9%	18.3%	20.4%	-9.7%
Free Cash Flow	131	376	420	504	589	411	461	209	280
Income Tax	-1	1	---	0	0	0	0	0	0

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	1956	2122	2285	2361	2193	2219	2395	2587	2166
Cash & Equivalents	28	94	25	33	40	7	244	36	56
Accounts Receivable	173	154	184	123	152	182	175	162	105
Inventories	47	44	83	121	61	60	59	101	56
Goodwill & Int. Ass.	---	---	---	136	136	136	136	136	4373
Total Liabilities	1251	1271	1270	1372	1100	1068	1207	1321	1094
Accounts Payable	100	79	86	84	64	97	96	81	48
Long-Term Debt	791	868	821	818	549	488	656	781	593
Shareholder's Equity	705	851	1015	987	1088	1146	1182	1253	1061

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	18.2%	19.3%	22.6%	13.2%	14.9%	13.8%	15.9%	16.0%	-5.4%
Return on Equity	50.5%	50.6%	53.3%	30.6%	32.7%	27.2%	31.5%	32.8%	-11.2%
ROIC	44.9%	47.4%	58.9%	37.3%	49.4%	57.9%	63.5%	54.9%	-18.5%
Shares Out.	73.7	73.9	74.0	74.2	74.4	98.7	130.8	128.1	127
Revenue/Share	27.59	29.84	31.07	30.65	25.98	18.20	15.32	15.31	10.44
FCF/Share	1.78	5.08	5.67	6.79	7.93	4.16	3.52	1.63	2.20

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

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