



# Suburban Propane (SPH)

Updated May 22<sup>nd</sup>, 2022, by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$16.54	<b>5 Year CAGR Estimate:</b>	12.7%	<b>Market Cap:</b>	\$1,050 M
<b>Fair Value Price:</b>	\$21	<b>5 Year Growth Estimate:</b>	1.0%	<b>Ex-Dividend Date:</b>	08/01/22 <sup>1</sup>
<b>% Fair Value:</b>	79%	<b>5 Year Valuation Multiple Estimate:</b>	4.9%	<b>Dividend Payment Date:</b>	08/09/22
<b>Dividend Yield:</b>	7.9%	<b>5 Year Price Target</b>	\$22	<b>Years Of Dividend Growth:</b>	1
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	B	<b>Rating:</b>	Buy

## Overview & Current Events

Suburban Propane has been in operation since 1928 and became a Master Limited Partnership in 1996. The partnership services most of the U.S. with propane and other energy sources, with propane making up around 90% of total revenue. It has a market capitalization of \$1,050 million and should generate about \$1.3 billion in revenue this year. The partnership has about 3,200 full-time employees in 41 states, serving approximately 1 million customers.

Suburban reported second quarter earnings on May 5<sup>th</sup>, 2022, and results were better than expected on both revenue and profits. Earnings-per-share came to \$2.74, which was 70 cents better than expected. That was up from \$2.03 in the year-ago period. Adjusted EBITDA, which is our preferred earnings measurement for Suburban, was up 0.3% to \$173 million.

Revenue was up 9.5% to \$588 million, which was attributable to a small decline in volume more than offset by a sizable increase in pricing. Retail propane gallons sold were 159 million, down 5.8% year-over-year, primarily due to record warm temperatures in December. In addition, Suburban cited unseasonably warm and inconsistent temperatures throughout the quarter, as well as customer conservation due to high commodity prices. Temperatures were 7% warmer than normal during the quarter in Suburban's service areas.

Average propane prices were up 45% year-over-year, and up 4.7% to the first quarter. Gross margin was \$349 million, up from \$306 million, although that included a \$33 million unrealized gain for mark-to-market adjustments.

Following Q2 results, we've boosted our estimate of CF/S to \$3.50 from \$3.30 on strong pricing.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>CF/S</b>	\$1.23	\$3.58	\$3.82	\$3.59	\$2.36	\$2.72	\$3.28	\$3.66	\$2.86	\$3.65	<b>\$3.50</b>	<b>\$3.68</b>
<b>DPS</b>	\$3.41	\$3.50	\$3.50	\$3.54	\$3.55	\$3.26	\$2.40	\$2.40	\$1.80	\$1.26	<b>\$1.30</b>	<b>\$1.82</b>
<b>Shares<sup>2</sup></b>	39	58	61	61	61	61	62	62	63	63	<b>63</b>	<b>64</b>

Cash flow has been predictably volatile during the past decade as it is all down to the weather for Suburban. It relies heavily upon heating demand so when temperatures are warmer than normal – as they have been for the past four years – results suffer. We forecast 1% average annual growth for the next five years as Suburban grapples with weather-related volumes but produces higher margins. Weather patterns deteriorated for Suburban during the most recent heating season, which is critical for earnings. Shareholders would do well to monitor Suburban's results on a quarterly basis for commentary from management on this key variable.

Suburban cut its distribution in fiscal 2018 after it became clear it was unsustainable, and again in fiscal 2020. However, we see a payout of \$1.82 per share by fiscal 2027 as the partnership's fundamentals appear to be stabilizing. Cash flow should cover the distribution in the coming years, so another cut should not be necessary. Of course, Suburban should have been able to cover the distribution prior to 2020's cut, so we continue to be cautious despite the increase in the payout that we're forecasting.

<sup>1</sup> Estimated date

<sup>2</sup> In millions

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## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/CF	18.2	7.5	7.3	7.3	9.9	8.0	7.1	6.2	6.2	4.2	4.7	6.0
Avg. Yld.	7.9%	7.9%	7.8%	8.5%	11.6%	12.1%	10.3%	10.5%	10.2%	8.2%	7.9%	8.3%

Suburban's valuation remains very low, and we see the stock as undervalued. A 4.9% annual tailwind from the rising valuation could meaningfully boost returns going forward, as shares trade for just 4.7 times CF/S. That compares quite favorably to our estimate of 6 times CF. We see the yield potentially rising slightly in the coming years given a potentially rising distribution.

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

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	80%	277%	98%	92%	99%	150%	120%	73%	63%	35%	37%	50%

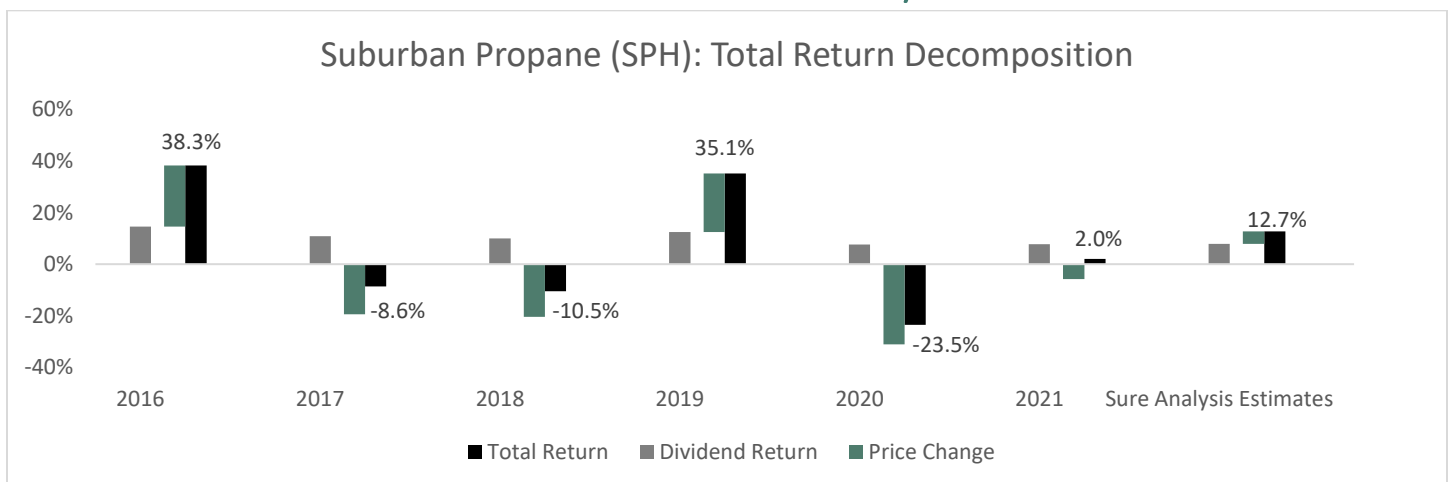
Suburban's payout ratio is very reasonable against its cash flow per share. Over time, we expect that to rise given that we see the distribution rising.

Suburban's main competitive advantages are its switching costs as well as its entrenched position in its service areas. It has a long operating history in the Northeast and that has allowed it to expand to other parts of the U.S., providing additional buying and distribution leverage. It is not beholden to economic conditions, so recessions are not a concern, but the weather is always a factor. It is not immune to competition as a natural gas distribution utility could encroach on Suburban's core business, especially if propane became significantly more expensive than natural gas. Suburban will likely need to continue acquiring smaller propane competitors to sustain its volumes as organic sales should continue to decline. This adds acquisition and integration risks to the operation as well.

## Final Thoughts & Recommendation

Overall, Suburban appears to be an attractive investment with its forecast annual returns of 12.7% thanks to its huge yield and tailwind from the valuation. Suburban is very attractive for income and value investors as the yield is still quite high, and the stock has a compelling valuation. The distribution should be safe at its current levels for the foreseeable future, offering income investors the chance to grab a sizable yield. Suburban is not without risks, but the current stock price and distribution seem to be pricing in these risks. Shares continue to earn a buy rating for investors who can stomach its weather-based volatility and elevated risk from high debt levels.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Revenue</b>	1,063	1,704	1,938	1,417	1,046	1,188	1,344	1,268	1,108	1,289
<b>Gross Profit</b>	464	842	858	824	684	711	752	746	725	803
<b>Gross Margin</b>	43.7%	49.4%	44.2%	58.1%	65.4%	59.9%	55.9%	58.8%	65.4%	62.3%
<b>SG&amp;A Exp.</b>	59	65	65	68	61	57	66	71	66	74
<b>D&amp;A Exp.</b>	47	130	136	133	130	128	125	121	117	105
<b>Operating Profit</b>	60	177	190	178	81	129	163	151	140	213
<b>Operating Margin</b>	5.6%	10.4%	9.8%	12.5%	7.7%	10.8%	12.1%	11.9%	12.7%	16.5%
<b>Net Profit</b>	1	79	95	84	14	38	77	69	61	123
<b>Net Margin</b>	0.1%	4.6%	4.9%	6.0%	1.4%	3.2%	5.7%	5.4%	5.5%	9.5%
<b>Free Cash Flow</b>	93	186	195	283	119	136	178	192	177	197
<b>Income Tax</b>	0	1	1	1	1	0	(1)	1	(0)	1

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Total Assets</b>	2,884	2,728	2,609	2,486	2,282	2,171	2,101	1,998	2,047	2,052
<b>Cash &amp; Equivalents</b>	134	107	93	152	37	3	5	2	3	6
<b>Accounts Receivable</b>	89	95	97	60	54	66	71	59	55	71
<b>Inventories</b>	88	78	91	48	45	53	59	45	47	62
<b>Goodwill &amp; Int. Ass.</b>	1,562	1,504	1,447	1,395	1,371	1,315	1,269	1,227	1,188	1,146
<b>Total Liabilities</b>	1,793	1,599	1,588	1,587	1,574	1,618	1,607	1,575	1,685	1,626
<b>Accounts Payable</b>	53	53	49	35	32	39	38	34	32	39
<b>Long-Term Debt</b>	1,422	1,245	1,243	1,241	1,225	1,272	1,255	1,227	1,210	1,118
<b>Shareholder's Equity</b>	1,090	1,129	1,021	898	708	553	494	424	362	425

## Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Return on Assets</b>	0.0%	2.8%	3.5%	3.3%	0.6%	1.7%	3.6%	3.3%	3.0%	6.0%
<b>Return on Equity</b>	0.1%	7.1%	8.8%	8.8%	1.8%	6.0%	14.6%	15.0%	15.5%	31.2%
<b>Shares Out.</b>	39	58	61	61	61	61	62	62	63	63
<b>Revenue/Share</b>	27.28	29.07	31.90	23.26	17.10	19.30	21.74	20.33	17.66	20.36
<b>FCF/Share</b>	2.40	3.18	3.22	4.65	1.95	2.20	2.87	3.08	2.82	3.11

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

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