Coterra Energy (CTRA)

Updated November 19th, 2022, by Thomas Richmond

Key Metrics

Current Price:	$27	**5 Year CAGR Estimate:**	11.8%	**Market Cap:**	$20.9 B
Fair Value Price:	$41	**5 Year Growth Estimate:**	1.0%	**Ex-Dividend Date:**	12/29/22
% Fair Value:	65%	**5 Year Valuation Multiple Estimate:**	8.9%	**Dividend Payment Date:**	01/27/23
Dividend Yield:	2.3%	**5 Year Price Target**	$43	**Years Of Dividend Growth:**	6
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Buy

Overview & Current Events

Coterra Energy (CTRA) is an oil and gas company that develops, explores, and produces oil, natural gas, and natural gas liquids. The business primarily operates in the Permian Basin, where the company is currently running 6 rigs and 2 completion crews, and the Marcellus Shale area, where the company is currently running 3 rigs and 1 completion crew. On October 1st, 2021, Coterra was formed through the combination of Cabot Oil & Gas (used to trade as COG) and Cimarex Energy (used to trade as XEC). With the new combined company, management believes they have built a diversified company with a strong free cash flow profile, and they expect to drive shareholder value by returning free cash flow to shareholders through dividends and share buybacks. Management is also targeting $100 million in G&A synergies from the merger. The business makes most of its money from natural gas (81% of 2021 sales) and oil (18% of 2021 sales).

On November 3rd, 2022, Coterra Energy reported Q3 2022 results for the period ending September 30th, 2022. The business earned $1.42 in adjusted earnings-per-share in the quarter, which beat analysts' estimates by 3 cents and represented 173.1% year-over-year growth in earnings-per-share. Revenue increased 472.2% year-over-year to $2.52 billion for the quarter, which beat analysts' estimates by $130 million. This quarter, management returned 74% of the third quarter's free cash flows to shareholders, with 50% of the returns coming from the combination of the base and variable dividend and 24% of the return coming from share repurchases. The company made a total of $1.06 billion in free cash flow for the quarter, and in the third quarter, the company paid a base dividend of $0.15 per share and a variable dividend of $0.53 per share.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$0.31	$0.66	$0.25	-$0.28	-$0.91	$0.22	$1.24	$1.63	$0.50	$2.29	***$5.10***	***$5.36***
DPS	$0.04	$0.05	$0.08	$0.08	$0.08	$0.17	$0.25	$0.35	$0.40	$0.46	***$0.60***	***$0.80***
Shares	422	422	418	414	457	466	448	418	401	504	***770***	***720***

As an oil and gas upstream business, the business' earnings are subject to the volatility of the oil market, which helps to explain the erratic earnings over the past decade. In 2022, we expect Coterra to deliver about $5.10 in earnings-per-share, and we forecast that earnings-per-share will increase slightly over the intermediate term. We forecast that the business will benefit in the short term from a favorable oil and gas environment due to Russian oil sanctions.

Even though we expect earnings-per-share might struggle to maintain this year's high level, we still think the business is going to benefit from the massive free cash flow generation from this boom period. The business has reported that they're looking to return at least 50% of quarterly free cash flow to shareholders going forward through variable dividends and share buybacks. This return policy guided our share count estimate, but the variable dividends were not included in our analysis of the company because they're not part of the regular dividend and we don't know how long the variable dividends will last. The annualized regular dividend for this year is currently $0.60 based on a $0.15 quarterly base dividend. Although this is Coterra's first year as a combined company, Coterra technically has a 6-year consecutive history of growing dividends, and a 31-year consecutive history of paying dividends.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	80.0	68.0	30.9	---	---	---	42.2	9.2	30.7	21.6	***5.2***	***8.0***
Avg. Yld.	3.7%	1.8%	1.7%	1.9%	2.6%	2.8%	2.7%	2.4%	3.5%	3.6%	***2.3%***	***1.9%***

As a cyclical business, Coterra Energy sees fluctuating earnings and fluctuating P/E ratios. We estimate that a P/E ratio of about 8 is fair for the business under normal conditions, so this guided our 2027 P/E estimate. Today, the stock offers a low regular dividend of $0.60 for the year, which works out to be a 2.3% dividend yield, but we expect the real dividend yield will probably be in the high single digits when factoring in the added variable dividend that helps to return more cash to shareholders. This is a high yield for investors, but investors should be careful if they're looking for sustainable dividend income because these variable dividends could decrease in the future.

Safety, Quality, Competitive Advantage, & Recession Resiliency

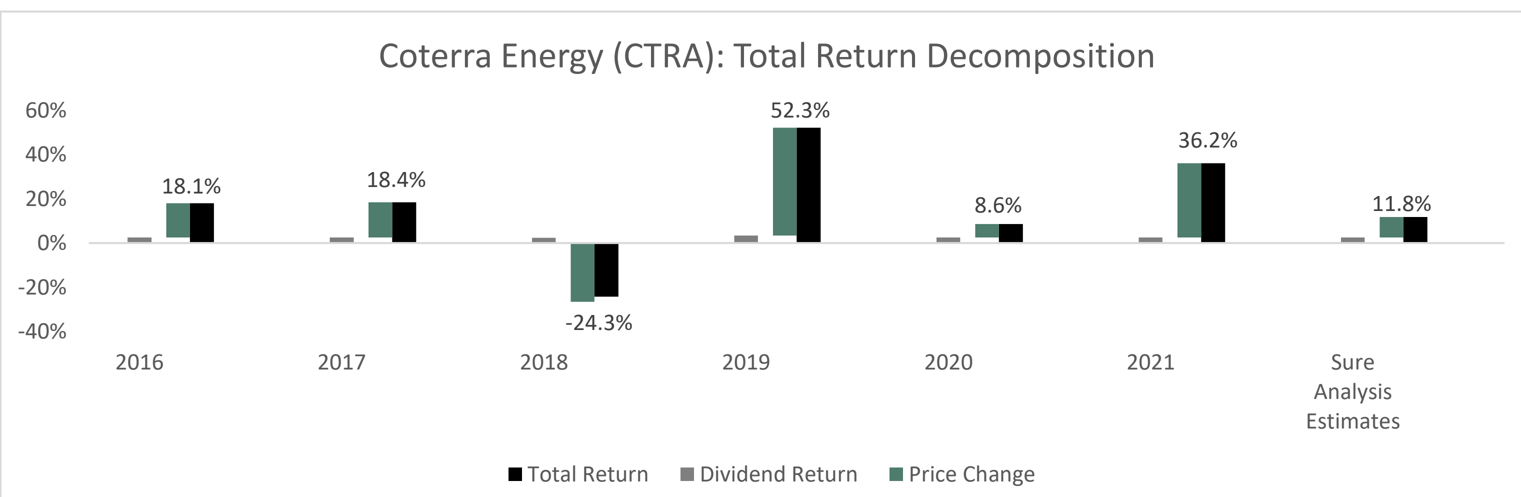
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	13%	8%	32%	---	---	77%	20%	21%	80%	20%	***12%***	***15%***

We consider the business's payout ratio to be safe because dividends are paid out from the company's cash flows. Additionally, the business has a strong balance sheet after the merger, with nearly $800 million in cash compared to about $2.3 billion in total debt and over $12.5 billion in shareholders' equity. The business has a competitive advantage as a company with a strong balance sheet and production in a time when oil prices are high. The business's strong balance sheet helps to give the company some recession resiliency, but the oil and gas industry is generally susceptible to economic downturns.

Final Thoughts & Recommendation

Coterra Energy is a business that is poised to benefit from oil and gas industry tailwinds. At today's price, we rate the stock as a Buy because total return prospects come in at 11.8% annually over the next five years, driven by a 2.3% dividend yield, an estimated 1% annual growth in earnings-per-share, and an estimated 8.9% annual return from the valuation multiple of the stock rerating higher. Investors might be interested in this company today because the business is returning a large amount of its free cash flows to shareholders through dividends and share buybacks, and now is a favorable time for the oil and gas industry.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	1,205	1,746	2,173	1,357	1,156	1,764	2,188	2,066	1,466	3,449
Gross Profit	463	695	1,015	154	18	596	1,020	1,008	431	1,937
Gross Margin	38.4%	39.8%	46.7%	11.3%	1.5%	33.8%	46.6%	48.8%	29.4%	56.2%
SG&A Exp.	121	105	83	68	86	98	97	95	106	164
D&A Exp.	---	---	---	---	---	---	---	406	391	693
Operating Profit	255	529	857	16	(125)	444	787	876	296	1,672
Op. Margin	21.2%	30.3%	39.4%	1.2%	-10.8%	25.1%	36.0%	42.4%	20.2%	48.5%
Net Profit	132	280	104	(114)	(417)	100	557	681	201	1,158
Net Margin	10.9%	16.0%	4.8%	-8.4%	-36.1%	5.7%	25.5%	33.0%	13.7%	33.6%
Free Cash Flow	(276)	(170)	(243)	(206)	22	134	210	657	202	939
Income Tax	106	206	(72)	(73)	(242)	(329)	141	219	41	344

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4,616	4,981	5,438	5,253	5,123	4,727	4,199	4,487	4,524	19,900
Cash & Equivalents	31	23	21	1	499	480	2	200	140	1,036
Acc. Receivable	165	215	228	117	186	216	363	209	216	922
Inventories	14	17	14	17	13	8	11	14	15	39
Total Liabilities	2,485	2,776	3,295	3,244	2,555	2,203	2,111	2,336	2,308	8,162
Accounts Payable	14	26	55	30	27	8	30	22	11	94
Long-Term Debt	1,087	1,147	1,752	2,016	1,521	1,522	1,226	1,220	1,134	3,125
Total Equity	2,131	2,205	2,143	2,009	2,568	2,524	2,088	2,151	2,216	11,738
LTD/E Ratio	0.51	0.52	0.82	1.00	0.59	0.60	0.59	0.57	0.51	0.27

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	2.9%	5.8%	2.0%	-2.1%	-8.0%	2.0%	12.5%	15.7%	4.5%	9.5%
Return on Equity	6.2%	12.9%	4.8%	-5.5%	-18.2%	3.9%	24.2%	32.1%	9.2%	16.6%
ROIC	4.2%	8.5%	2.9%	-2.9%	-10.3%	2.5%	15.1%	20.4%	6.0%	12.7%
Shares Out.	422	422	418	414	457	466	448	418	401	504
Revenue/Share	2.85	4.13	5.20	3.28	2.53	3.79	4.89	4.94	3.66	6.84
FCF/Share	(0.65)	(0.40)	(0.58)	(0.50)	0.05	0.29	0.47	1.57	0.50	1.86

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