Genesis Energy (GEL)

Updated November 7th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	$11	**5 Year CAGR Estimate:**	10.7%	**Market Cap:**	$1.4 B
Fair Value Price:	$12	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	10/28/2022
% Fair Value:	92%	**5 Year Valuation Multiple Estimate:**	1.8%	**Dividend Payment Date:**	11/14/2022
Dividend Yield:	5.5%	**5 Year Price Target**	$15	**Years Of Dividend Growth:**	0
Dividend Risk Score:	D	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

Genesis Energy is a diversified midstream energy limited partnership, which generates 48% of its operating income from offshore pipeline transportation, 29% from sodium minerals and sulfur services, 17% from onshore facilities and 6% from marine transportation. It has a market capitalization of $1.4 billion.

Genesis Energy has dramatically underperformed the market in the last five years, as shares have fallen -52% whereas the S&P has rallied 45%. The underperformance of Genesis Energy reflects its poor business performance. The MLP has spent hefty amounts on capital expenses but the performance of its investments has been poor. As a result, it has posted negative free cash flows in five out of the last eight years. Moreover, it has diluted its unit holders, as it has increased its unit count by 56% in the last nine years. Furthermore, it has markedly increased its debt load, with its interest expense currently exceeding its operating income. Consequently, when some turnarounds and Hurricane Harvey adversely affected its results, the MLP was forced to cut its distribution by -31% in late 2017.

Even worse, Genesis Energy faced a fierce downturn in 2020-2021 due to the pandemic, which severely hurt the oil segment and the sodium business. The MLP cut its quarterly distribution by -73% in 2020, from $0.55 to $0.15.

In late October, Genesis Energy reported (10/27/22) financial results for the third quarter of fiscal 2022. The offshore pipeline remained in recovery mode and the soda business continued to recover from the pandemic, with increased demand resulting in material price hikes. As a result, Genesis Energy switched from a loss per unit of -$0.17 in last year's quarter to a profit per unit of $0.03. Moreover, Genesis Energy posted distributable cash flow of $92.6 million and thus it posted a strong distribution coverage ratio of 5.0. Management expects a continued recovery in volumes in the Gulf of Mexico and in the soda business and thus it now expects adjusted EBITDA of $700-$710 million in the full year. Nevertheless, the hefty loss in 2020, which was ~36% of the current market cap, is a stern reminder of the excessive risk of Genesis Energy in the event of a prolonged downturn.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
DCF/U	$1.94	$1.68	$2.07	$2.18	$2.81	$2.52	-$4.22	$2.93	$2.08	$1.66	***$2.40***	***$3.06***
DPU	$1.87	$2.07	$2.29	$2.47	$2.72	$2.65	$2.10	$2.20	$1.00	$0.60	***$0.60***	***$0.60***
Shares[1]	78.4	84.0	90.1	103.0	113.4	121.5	122.6	122.6	122.6	122.6	***122.6***	***150.0***

Genesis Energy has failed to grow its DCF per unit over the last decade, mostly due to its poor investments and the impact of the pandemic on its business. The MLP has net debt of $3.8 billion, which is 2.7 times the current market cap, and a high leverage ratio (net debt/EBITDA) of 4.3. Due to its high leverage, the MLP was forced to sell a 36% stake in its CHOPS oil pipeline system in 2021 and used the proceeds to pay debt and become compliant with the requirements of its lenders. Due to an expected recovery from the pandemic, we expect 5.0% growth of DCF per unit on average over the next five years. Part of this growth should come from the deleveraging process, which will reduce interest expense to healthier levels. The choppy and poor growth record raises a red flag for the stock.

[1] 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	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/DCF	18.4	31.3	20.5	16.9	12.9	8.9	---	7.3	3.8	5.7	***4.6***	***5.0***
Avg. Yld.	6.0%	4.2%	4.4%	5.7%	8.1%	8.8%	9.4%	9.4%	12.5%	6.3%	***5.5%***	***3.9%***

Genesis Energy is currently trading at a P/DCF ratio of 4.6, which is lower than its historical 5-year average of 6.4. However, as Genesis Energy currently has a high debt load, we assume a fair DCF multiple of 5.0. If the stock trades at this valuation level in five years, it will enjoy a 1.8% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

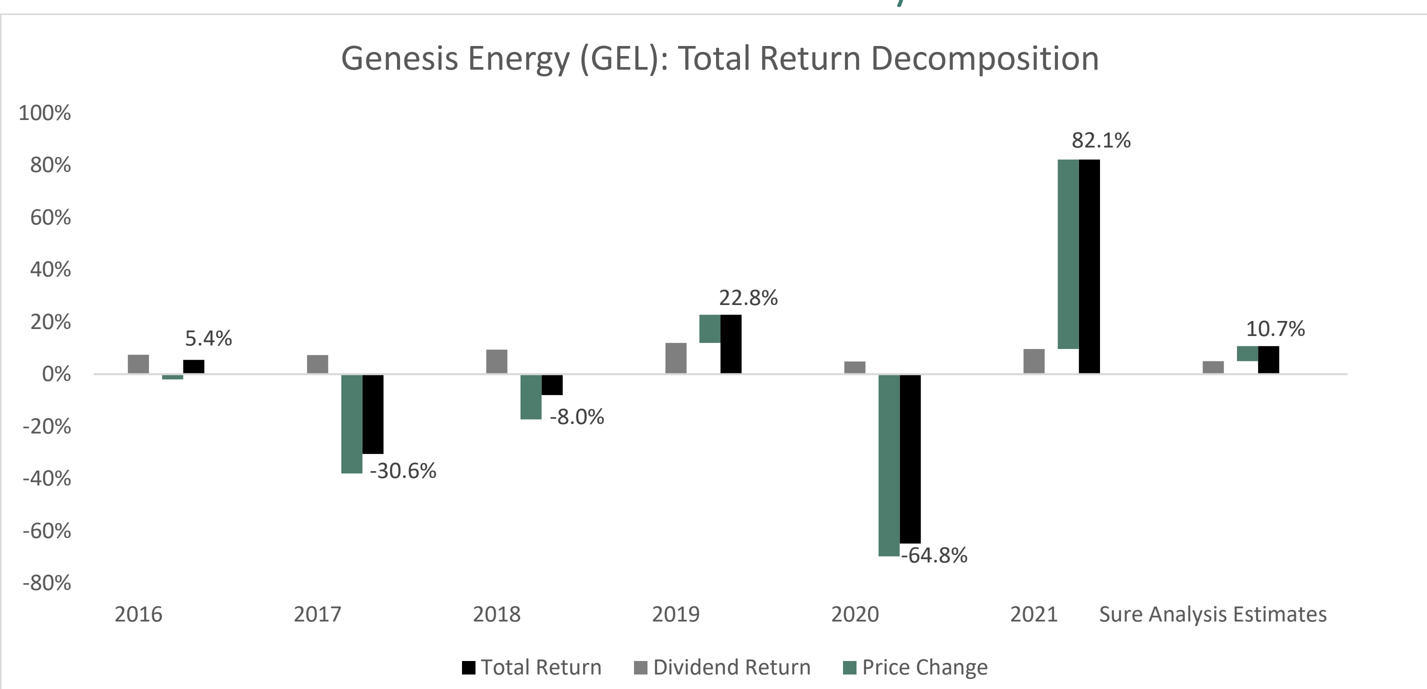
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	77.0%	87.7%	78.7%	37.6%	66.2%	65.0%	38.2%	75.1%	48.0%	36.1%	***25.0%***	***19.6%***

Given the volatile and lackluster performance record of Genesis Energy, it is evident that there is no meaningful competitive advantage in place. While Genesis Energy operates primarily with a fee-based model, its earnings are not resilient. In our view, the MLP invested too heavily and increased its leverage too much in the past. As a result, the financial burden of its debt exerts a strong drag on its results through high interest expense and dilution of its unit holders. It also renders Genesis Energy highly vulnerable to any downturn in its business, such as a recession.

Final Thoughts & Recommendation

Due to its poor business performance and its high leverage, which has caused two distribution cuts, Genesis Energy has dramatically underperformed the market in the last five years. However, the stock can offer a 10.7% average annual return over the next five years thanks to its 5.5% distribution, 5.0% growth and a 1.8% valuation tailwind. Nevertheless, it will be highly vulnerable in the event of another downturn, such as a recession. We rate the stock as a hold only for those who realize its risk and can stomach high stock price volatility.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	3,367	4,135	3,846	2,247	1,712	2,028	2,913	2,481	1,825	2,125
Gross Profit	157	158	183	222	252	247	321	325	114	137
Gross Margin	4.6%	3.8%	4.8%	9.9%	14.7%	12.2%	11.0%	13.1%	6.2%	6.4%
SG&A Exp.	42	47	51	65	46	66	67	53	57	61
D&A Exp.	61	65	91	---	---	---	---	---	---	---
Operating Profit	115	111	133	139	206	164	259	273	57	76
Operating Margin	3.4%	2.7%	3.4%	6.2%	12.1%	8.1%	8.9%	11.0%	3.1%	3.6%
Net Profit	96	86	106	423	113	83	(6)	96	(417)	(165)
Net Margin	2.9%	2.1%	2.8%	18.8%	6.6%	4.1%	-0.2%	3.9%	-22.8%	-7.8%
Free Cash Flow	43	(205)	(152)	(206)	(180)	73	195	219	153	37
Income Tax	(9)	1	3	4	3	(4)	1	1	1	2

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	2,110	2,862	3,211	5,460	5,703	7,137	6,479	6,598	5,934	5,906
Cash & Equivalents	11	9	9	11	7	9	10	29	27	20
Accounts Receivable	271	368	272	220	225	495	323	417	392	400
Inventories	87	85	47	44	99	89	74	65	100	78
Goodwill & Int. Ass.	400	388	408	548	530	507	465	441	431	429
Total Liabilities	1,193	1,764	1,981	3,439	3,583	4,423	4,037	4,376	4,325	3,926
Accounts Payable	258	316	245	141	120	271	127	219	198	264
Long-Term Debt	851	1,284	1,581	2,922	3,091	3,698	3,432	3,429	3,394	2,980
Shareholder's Equity	916	1,098	1,229	2,029	2,130	2,723	2,453	2,225	1,610	1,426

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	5.0%	3.5%	3.5%	9.7%	2.0%	1.3%	-0.1%	1.5%	-6.7%	-2.8%
Return on Equity	11.3%	8.6%	9.1%	25.9%	5.4%	3.4%	-0.2%	4.1%	-21.7%	-10.9%
Shares Out.	78.4	84.0	90.1	103.0	113.4	121.5	122.6	122.6	122.6	122.6
Revenue/Share	42.97	49.25	42.71	21.81	15.10	16.69	23.76	20.24	14.89	17.34
FCF/Share	0.55	-2.44	-1.69	-2.00	-1.59	0.60	1.59	1.79	1.25	0.30

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