



# Atmos Energy Corp. (ATO)

Updated February 14<sup>th</sup>, 2023, by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$117	<b>5 Year CAGR Estimate:</b>	7.9%	<b>Market Cap:</b>	\$16.7 B
<b>Fair Value Price:</b>	\$114	<b>5 Year Growth Estimate:</b>	6.0%	<b>Ex-Dividend Date:</b>	02/17/23
<b>% Fair Value:</b>	103%	<b>5 Year Valuation Multiple Estimate:</b>	-0.5%	<b>Dividend Payment Date:</b>	03/06/23
<b>Dividend Yield:</b>	2.5%	<b>5 Year Price Target</b>	\$153	<b>Years Of Dividend Growth:</b>	39
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	B	<b>Rating:</b>	Hold

## Overview & Current Events

Atmos Energy can trace its beginnings all the way back to 1906 when it was formed in Texas. Since that time, it has grown both organically and through mergers to a \$16.7 billion market capitalization. The company distributes and stores natural gas in eight states, serves over 3 million customers, and should generate about \$4.3 billion in revenue this year. Atmos has a 39-year history of raising dividends, putting it in rare company among dividend stocks.

Atmos reported first quarter earnings on February 7<sup>th</sup>, 2023, and results were somewhat mixed. Earnings-per-share came to \$1.91, which was four cents less than expected. However, revenue was up 47% to \$1.48 billion, beating estimates by \$340 million.

Consolidated operating income was up \$45 million to \$321 million for the quarter. This was primarily due to rate outcomes in both of the company's segments, as well as customer growth in the distribution segment. This was partially offset by increased operation and maintenance costs, as well as higher depreciation and property tax expenses, due to higher capital investments.

Distribution operating income was up \$41 million to \$232 million, which was due to a \$58 million gain from rates, a \$6 million decline from refunds of excess deferred taxes, and customer growth of \$2 million. This was partially offset by higher operating and maintenance expense.

Pipeline and storage operating income rose \$4 million to \$89 million. This was due to higher rates, which were somewhat offset by higher operating and maintenance costs.

We reiterate our estimate of \$6.00 in earnings-per-share for this year.

## Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
<b>EPS</b>	\$2.50	\$2.96	\$3.09	\$3.38	\$3.60	\$4.00	\$4.35	\$4.69	\$5.12	\$5.60	<b>\$6.00</b>	<b>\$8.03</b>
<b>DPS</b>	\$1.40	\$1.48	\$1.56	\$1.68	\$1.80	\$1.94	\$2.10	\$2.30	\$2.57	\$2.72	<b>\$2.96</b>	<b>\$4.35</b>
<b>Shares<sup>1</sup></b>	90	91	100	101	104	106	117	123	132	140	<b>140</b>	<b>140</b>

Atmos' earnings-per-share has risen steadily in the past decade as the company continues to grow both organically and through acquisitions. We are forecasting a five-year annual growth rate of 6% moving forward, in line with our prior estimate.

The company can achieve this growth through continued improvements in gross margin, reductions in operating costs as a percentage of revenue, and top line growth via acquisitions as well as customer growth. Along with margin improvements, Atmos should be able to produce mid-to-upper single-digit earnings-per-share growth annually. It continues to file favorable rate cases with its various localities that provide for small revenue increases over time as well, as we saw again in 2020 full-year results, and indeed in 2021 and 2022 results. The distribution segment continues to lead the way while pipeline and storage struggles.

<sup>1</sup> Share count 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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We are forecasting similar growth for the dividend as years of weak dividend growth have given way to a management team that is more willing to boost the payout. The company's payout ratio is much lower than it has been in the past and thus a dividend growth rate congruent with earnings-per-share growth, or slightly higher, looks reasonable given recent history. Indeed, the most recent dividend increase was 8.8%. We see the dividend rising to \$4.35 over the next five years.

## Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	15.9	16.1	17.5	20.8	22.0	21.8	23.5	22.4	18.8	18.2	19.5	19.0
Avg. Yld.	3.5%	3.1%	2.9%	2.4%	2.3%	2.2%	2.0%	2.2%	2.7%	2.7%	2.5%	2.9%

Atmos, like many other utilities and dividend stocks in general, has seen a sizable increase in its valuation in recent years. Shares are valued more cheaply than at our last update, and stand today at 19.5 times this year's earnings. Thus, we are forecasting a small headwind to total returns based upon a return to a more normalized valuation level of a price-to-earnings ratio of 19. We see the yield potentially rising from 2.5% to 2.9% in the coming years.

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

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	56%	50%	51%	50%	50%	49%	48%	49%	50%	49%	49%	54%

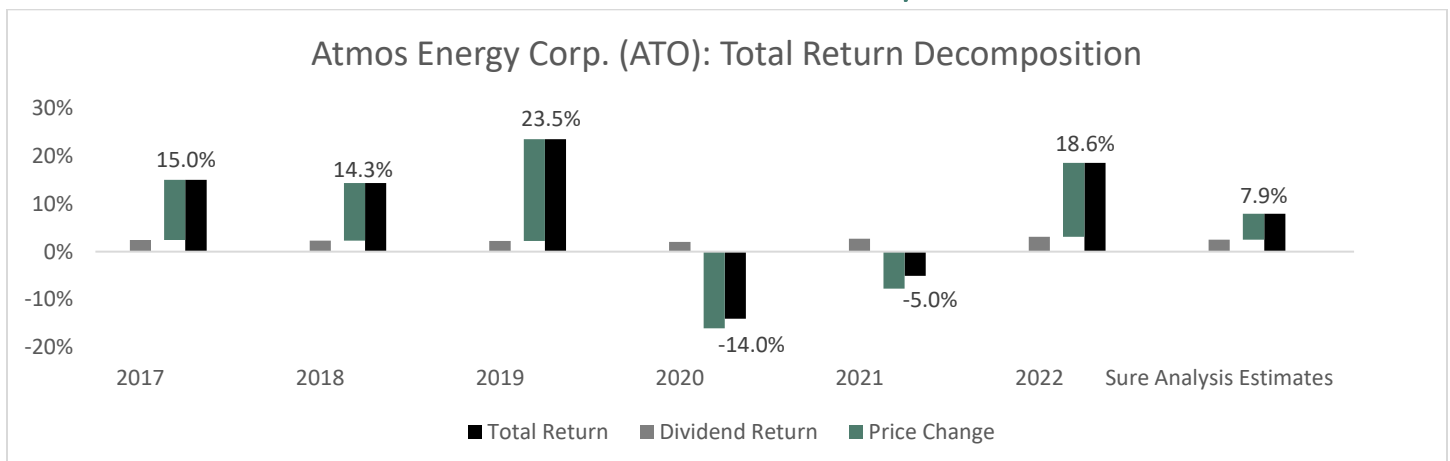
Atmos' payout ratio has drifted lower in recent years as dividend increases have been a lower priority than other spending. We expect the payout ratio to remain around 50% or slightly higher, as dividend increases roughly match the growth rate of earnings in the coming years. Atmos' dividend is safe and with the 2.5% yield, we see the payout as attractive compared to the broader market.

The company's competitive advantage is in its wide distribution area and lack of direct competition in its service areas for residential and commercial customers. In addition, discretionary use of natural gas is low as people use what they need, regardless of economic conditions, meaning Atmos' recession performance is likely to be resilient, as seen in 2020.

## Final Thoughts & Recommendation

Atmos has strong fundamentals and a long track record of solid performance, but the valuation has moderated of late. We are forecasting total annual returns of 7.9%, consisting of the current 2.5% yield, 6% earnings-per-share growth and a 0.5% potential headwind from the valuation. Given this, we're reiterating the stock at a hold rating.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Revenue</b>	3875	4941	2927	2455	2760	3116	2902	2,821	3,407	4,202
<b>Gross Profit</b>	1412	1582	1631	1708	1834	1948	2043	2,162	2,375	2,519
<b>Gross Margin</b>	36.4%	32.0%	55.7%	69.6%	66.5%	62.5%	70.4%	76.6%	69.7%	59.9%
<b>D&amp;A Exp.</b>	238	254	275	293	320	361	391	430	478	536
<b>Operating Profit</b>	502	611	612	657	736	728	746	824	905	921
<b>Operating Margin</b>	13.0%	12.4%	20.9%	26.8%	26.7%	23.4%	25.7%	29.2%	26.6%	21.9%
<b>Net Profit</b>	243	290	315	350	396	603	511	601	666	774
<b>Net Margin</b>	6.3%	5.9%	10.8%	14.3%	14.4%	19.4%	17.6%	21.3%	19.5%	18.4%
<b>Free Cash Flow</b>	-232	-92	-152	-292	-270	-343	-725	-898	-3,054	-1,467
<b>Income Tax</b>	143	187	190	197	221	8	139	145	154	78

## Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Total Assets</b>	7934	8595	9075	10011	10750	11874	13368	15,359	19,609	22,193
<b>Cash &amp; Equivalents</b>	66	42	29	48	26	14	25	21	117	52
<b>Accounts Receivable</b>	231	263	205	120	135	139	127	140	343	258
<b>Inventories</b>	250	285	249	185	189	174	136	119	178	384
<b>Goodwill &amp; Int. Ass.</b>	741	742	743	727	730	730	731	731	731	731
<b>Total Liabilities</b>	5354	5508	5880	6548	6851	7104	7617	8,568	11,702	12,774
<b>Accounts Payable</b>	70	78	79	114	143	135	177	141	423	259
<b>Long-Term Debt</b>	2824	2653	2895	3269	3515	3644	3994	4,523	4,930	8,095
<b>Shareholder's Equity</b>	2580	3086	3195	3463	3899	4770	5750	6,791	7,907	9,419
<b>LTD/E Ratio</b>	1.09	0.86	0.91	0.94	0.90	0.76	0.69	0.67	0.62	0.86

## Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Return on Assets</b>	3.2%	3.5%	3.6%	3.7%	3.8%	5.3%	4.1%	4.2%	3.8%	3.7%
<b>Return on Equity</b>	9.8%	10.2%	10.0%	10.5%	10.8%	13.9%	9.7%	9.6%	9.1%	8.9%
<b>ROIC</b>	4.7%	5.2%	5.3%	5.5%	5.6%	7.6%	5.6%	5.7%	5.0%	4.8%
<b>Shares Out.</b>	90	91	100	101	104	106	117	123	130	138
<b>Revenue/Share</b>	42.26	50.62	28.73	23.71	26.01	28.06	24.70	22.96	26.24	30.43
<b>FCF/Share</b>	-2.53	-0.94	-1.49	-2.82	-2.54	-3.09	-6.17	-7.31	-23.52	-10.62

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

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