Coterra Energy (CTRA)

Updated November 9th, 2023, by Aristofanis Papadatos

Key Metrics

Current Price:	$27	**5 Year CAGR Estimate:**	-1.5%	**Market Cap:**	$20.7 B
Fair Value Price:	$21	**5 Year Growth Estimate:**	0.0%	**Ex-Dividend Date:**	11/15/23
% Fair Value:	130%	**5 Year Valuation Multiple Estimate:**	-5.1%	**Dividend Payment Date:**	11/30/23
Dividend Yield:	3.0%	**5 Year Price Target**	$21	**Years Of Dividend Growth:**	7
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Sell

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, the Marcellus Shale area and the Anadarko Basin. The business makes most of its money from natural gas (86% of 2022 output) and to a lesser extent from oil (14% of 2022 output). The proved reserves of the company are approximately 78% natural gas, 10% oil and 12% natural gas liquids (NGLs). Overall, Coterra Energy is extremely sensitive to the dramatic cycles of the price of natural gas.

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 to have built a diversified company with a strong free cash flow profile, and expects to enhance 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.

In early November, Coterra Energy reported (11/6/23) financial results for the third quarter of fiscal 2023. The average realized price of gas grew sequentially thanks to the surge of consumption to an all-time high. As a result, earnings-per-share grew 28% sequentially, from $0.39 to $0.50, and exceeded the analysts' estimates by $0.07. The company has exceeded the analysts' estimates for 7 consecutive quarters. Thanks to its rich free cash flows, it has raised its regular dividend by 33% this year. However, its proved reserves declined -17% in 2022. This raises a red flag for the future growth prospects. In addition, due to an abnormally warm winter in the U.S. and Europe, the price of natural gas has incurred a sharp correction during the fourth quarter. As a result, we have lowered our forecast for annual earnings-per-share from $3.00 to $2.60.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$0.66	$0.25	-$0.28	-$0.91	$0.22	$1.24	$1.63	$0.50	$2.29	$4.94	***$2.60***	***$2.60***
DPS	$0.05	$0.08	$0.08	$0.08	$0.17	$0.25	$0.35	$0.40	$0.46	$0.60	***$0.80***	***$0.88***
Shares	422	418	414	457	466	448	418	401	504	781	***780***	***1000***

As a primarily gas upstream company, Coterra Energy is extremely sensitive to the swings of gas prices. This is clearly reflected in the highly volatile performance record of the company. Coterra Energy is currently thriving thanks to the sanctions imposed by western countries on Russia. Before the sanctions, Russia was producing about one-third of natural gas consumed in Europe. As a result, the sanctions greatly tightened the global gas market and led gas prices to skyrocket last year.

However, gas prices have deflated this year due to an abnormally warm winter in the U.S. and Europe. Moreover, there is a record number of renewable energy projects that are under development all over the world right now. When all these projects come online, they are likely to take their toll on the prices of oil and gas. Overall, we prefer to be cautious and assume that Coterra Energy will post essentially flat earnings-per-share in 2028 vs. 2023. While the company is likely to keep thriving in the short run, investors should never forget the dramatic cyclicality of this business.

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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	68.0	30.9	---	---	---	42.2	9.2	30.7	21.6	5.4	***10.4***	***8.0***
Avg. Yld.	1.8%	1.7%	1.9%	2.6%	2.8%	2.7%	2.4%	3.5%	3.6%	2.3%	***3.0%***	***4.2%***

As a cyclical business, Coterra Energy has fluctuating earnings and fluctuating price-to-earnings ratios. We estimate that a price-to-earnings ratio of about 8.0 is fair for the company under normal conditions. The stock is currently trading at a price-to-earnings ratio of 10.4. If it trades at our assumed fair valuation level in five years, it will incur a -5.1% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

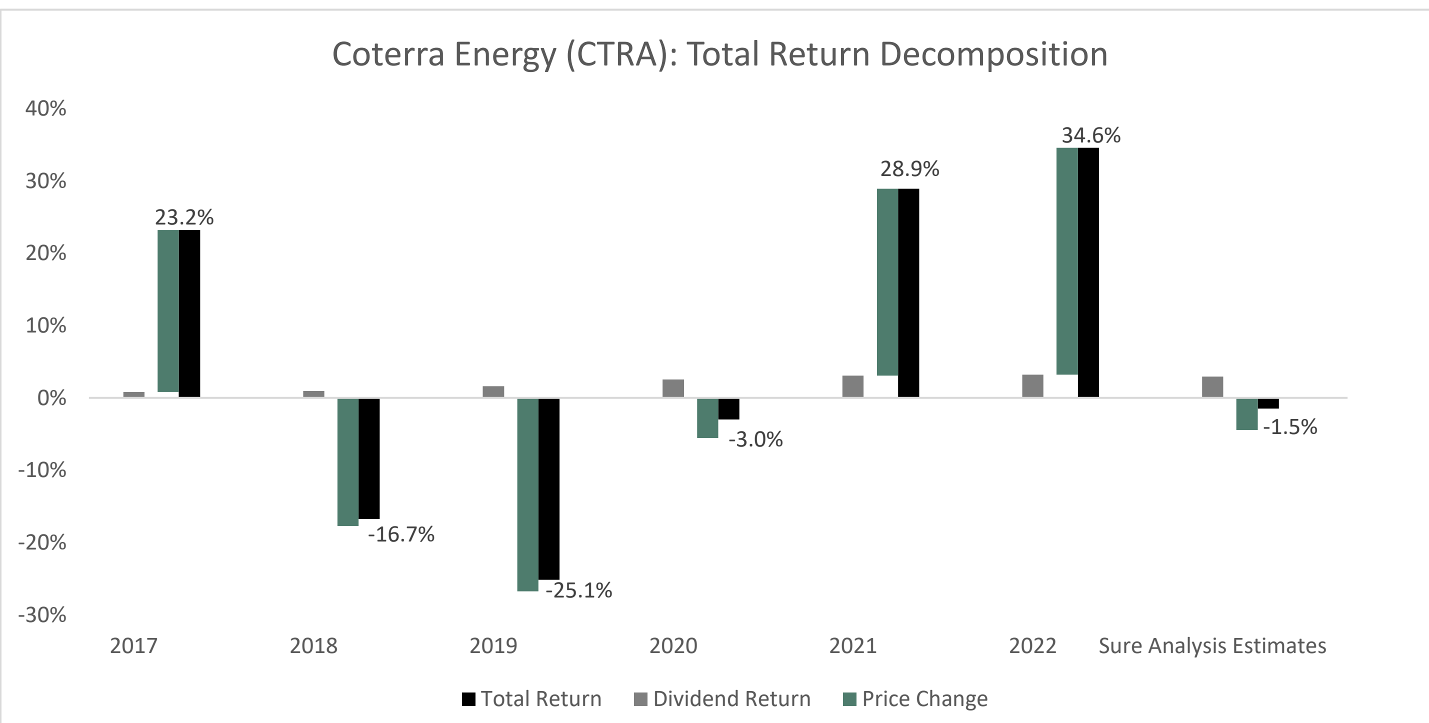
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	8%	32%	---	---	77%	20%	21%	80%	20%	12%	***31%***	***34%***

Coterra Energy has a strong balance sheet, which will help the company endure a potential downturn in its business. However, the company is highly vulnerable to the downturns of the energy sector, as its earnings are extremely sensitive to the price of natural gas. Consequently, the stock is not suitable for income-oriented investors. It is suitable only for investors with a strong conviction for higher gas prices in the future.

Final Thoughts & Recommendation

Coterra Energy is a company that is positioned to benefit from potentially high gas prices in the future. However, we view the stock as unattractive right now, especially given that we have passed the peak of the natural gas market. The stock could offer a -1.5% average annual return over the next five years, as its 3.0% starting dividend yield may be offset by a -5.1% potential valuation headwind. We thus maintain our sell rating.

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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	1,746	2,173	1,357	1,156	1,764	2,188	2,066	1,466	3,449	9,051
Gross Profit	695	1,015	154	18	596	1,020	1,008	431	1,937	7,636
Gross Margin	39.8%	46.7%	11.3%	1.5%	33.8%	46.6%	48.8%	29.4%	56.2%	84.4%
SG&A Exp.	105	83	68	86	98	97	95	106	164	327
D&A Exp.	---	---	---	---	---	---	406	391	693	1,635
Operating Profit	529	857	16	(125)	444	787	876	296	1,672	5,279
Op. Margin	30.3%	39.4%	1.2%	-10.8%	25.1%	36.0%	42.4%	20.2%	48.5%	58.3%
Net Profit	280	104	(114)	(417)	100	557	681	201	1,158	4,065
Net Margin	16.0%	4.8%	-8.4%	-36.1%	5.7%	25.5%	33.0%	13.7%	33.6%	44.9%
Free Cash Flow	(170)	(243)	(206)	22	134	210	657	202	939	3,746
Income Tax	206	(72)	(73)	(242)	(329)	141	219	41	344	1,104

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	4,981	5,438	5,253	5,123	4,727	4,199	4,487	4,524	19,900	20,154
Cash & Equivalents	23	21	1	499	480	2	200	140	1,036	673
Acc. Receivable	215	228	117	186	216	363	209	216	922	1,067
Inventories	17	14	17	13	8	11	14	15	39	63
Total Liabilities	2,776	3,295	3,244	2,555	2,203	2,111	2,336	2,308	8,162	7,495
Accounts Payable	26	55	30	27	8	30	22	11	94	27
Long-Term Debt	1,147	1,752	2,016	1,521	1,522	1,226	1,220	1,134	3,125	2,181
Total Equity	2,205	2,143	2,009	2,568	2,524	2,088	2,151	2,216	11,738	12,659
LTD/E Ratio	0.52	0.82	1.00	0.59	0.60	0.59	0.57	0.51	0.27	0.17

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	5.8%	2.0%	-2.1%	-8.0%	2.0%	12.5%	15.7%	4.5%	9.5%	20.3%
Return on Equity	12.9%	4.8%	-5.5%	-18.2%	3.9%	24.2%	32.1%	9.2%	16.6%	33.3%
ROIC	8.5%	2.9%	-2.9%	-10.3%	2.5%	15.1%	20.4%	6.0%	12.7%	27.4%
Shares Out.	422	418	414	457	466	448	418	401	504	799
Revenue/Share	4.13	5.20	3.28	2.53	3.79	4.89	4.94	3.66	6.84	11.33
FCF/Share	(0.40)	(0.58)	(0.50)	0.05	0.29	0.47	1.57	0.50	1.86	4.69

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