



Southwest Gas Holdings (SWX)

Updated November 16th, 2023 by Quinn Mohammed

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|------------|
| Current Price: | \$60 | 5 Year CAGR Estimate: | 5.6% | Market Cap: | \$4.4 B |
| Fair Value Price: | \$51 | 5 Year Growth Estimate: | 5.0% | Ex-Dividend Date: | 11/14/2023 |
| % Fair Value: | 117% | 5 Year Valuation Multiple Estimate: | -3.1% | Dividend Payment Date: | 12/01/2023 |
| Dividend Yield: | 4.1% | 5 Year Price Target: | \$65 | Years of Dividend Growth: | 15 |
| Dividend Risk Score: | C | Retirement Suitability Score: | C | Rating: | Hold |

Overview & Current Events

Southwest Gas Holdings Inc. is a holding company that operates in two business segments, Natural Gas Operations and Utility Infrastructure Services. The Natural Gas business, Southwest Gas Corp., purchases, distributes and transports natural gas in Arizona, California and Nevada and serves over 2 million customers. The corporation also owns and operates an interstate pipeline through their subsidiary Paiute Pipeline Company. Paiute also runs a peak shaving LNG storage facility. The Utility business, Centuri Group Inc. delivers a multitude of energy solutions to North America's gas and electric providers. Centuri operates across the U.S. and Canada.

The holdings company trades under the ticker symbol SWX on the NYSE and has a market capitalization of \$4.4 billion. Southwest Gas Holdings Inc. is headquartered in Las Vegas, Nevada. Its regulated natural gas utility, Southwest, was incorporated in March 1931.

On August 27th, 2021, SouthWest Gas completed the acquisition of Riggs Distler to expand Centuri's offerings. The acquisition diversifies Centuri's utility services platform, and add opportunities for growth in electric utility services, renewable energy, and 5G telecom.

On February 14th, 2023, SouthWest completed the sale of MountainWest, and used the proceeds to reduce debt. Furthermore, Southwest Gas is actively pursuing the spin-off of Centuri, its fully owned subsidiary, to create a new independent publicly traded utility infrastructure services company.

Southwest Gas Holdings reported third quarter 2023 results on November 8th, 2023, for the period ending September 30th, 2023. SWX reported diluted earnings per share of \$0.04 for Q3 compared to (\$0.18) per share in the year-ago quarter. Adjusted EPS soared to \$0.10 from a loss of (\$0.05) a year ago.

Growth on a Per-Share Basis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$3.11 | \$3.01 | \$2.92 | \$3.18 | \$4.04 | \$3.68 | \$3.94 | \$4.14 | \$4.00 | \$3.00 | \$2.85 | \$3.64 |
| DPS | \$1.29 | \$1.43 | \$1.58 | \$1.76 | \$1.94 | \$2.06 | \$2.16 | \$2.26 | \$2.36 | \$2.46 | \$2.48 | \$2.74 |
| Shares¹ | 46.5 | 46.5 | 47.4 | 47.5 | 48.1 | 53.0 | 55.0 | 56.9 | 60.6 | 67.2 | 72.0 | 85.0 |

Southwest Gas has grown its business fairly consistently over the past decade into 2021. For the nine and five years leading up to 2021, Southwest grew its earnings-per-share by roughly 1.9% and 1.3%, respectively.

The share count has also grown steadily, at a moderate pace, with 4.2% annual share count growth since 2013.

With the acquisition of Riggs Distler, upcoming regulated rate increases, expansion projects, increasing operating margin, and customer additions, Southwest should see earnings per share growth come in at around 5.0% per annum in the intermediate term. We expect the dividend to grow at about half of earnings by around 2%, as the payout has been eclipsing its historical range between 40% to 60%. The sale of MountainWest and the spin-off of Centuri should see Southwest Gas as a more efficient and nimble company in the coming years.

¹ In millions

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Valuation Analysis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | Now | 2028 |
|-----------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| Avg. P/E | 16.0 | 18.1 | 19.3 | 22.7 | 25.0 | 18.0 | 22.5 | 18.3 | 15.3 | 27.9 | 21.0 | 18.0 |
| Avg. Yld. | 2.5% | 2.5% | 2.7% | 2.4% | 2.3% | 2.7% | 2.5% | 3.2% | 3.4% | 3.0% | 4.1% | 4.2% |

The current P/E of 21.0 is above Southwest's historical PE ratio. In the past nine years, the average PE was 20.3. In the past five years, this average PE was 20.4. We peg fair value at 18.0 times earnings, which implies the potential for a moderate valuation contraction.

Safety, Quality, Competitive Advantage, & Recession Resiliency

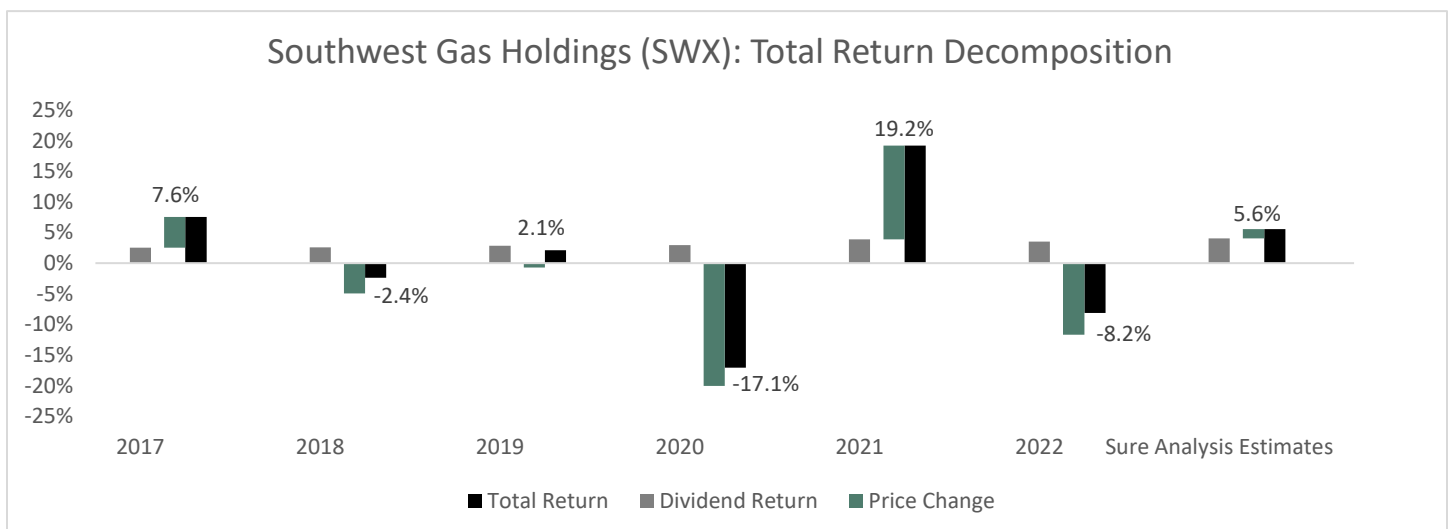
| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|--------|------|------|------|------|------|------|------|------|------|------|------------|------------|
| Payout | 41% | 47% | 54% | 55% | 48% | 56% | 55% | 54% | 59% | 82% | 87% | 75% |

The payout ratio historically has been below 60% and we see this being eclipsed in the next few years, but the dividend still appears to be safe, barring a significant downturn. Utilities businesses are generally safe during a recession, especially Southwest Gas, who primarily provides energy to residential customers. The corporation provides a necessary product, and not simply a want, so it is not likely to lose a lot of business, even through a recession. While the company has resiliency during a recession, it is not immune, and in the great financial crisis, earnings dropped 25% at the worst point. The company surpassed the earnings prior to the financial crisis in only one year and has remained above those earnings levels since. Southwest believes it has an advantage by communicating directly with home builders and commercial property developers to recommend natural gas appliances be installed in new builds, and thus is successful in providing many of these new homes with natural gas for the lifetime of the property and increase customer growth. The company also prefers to remain uninvolved in cross-country pipeline and electric transmission projects, likely due to strict regulations in getting these projects off the ground, which could be costly.

Final Thoughts & Recommendation

Southwest Gas Holdings is a strong, consistent, and fairly recession-resistant business. So far, the corporation has increased its dividend for fifteen consecutive years, and we see this continuing into the future. We estimate that the company is trading at 117% of fair value today and could produce 5.6% annualized total returns in the next five years. We estimate 5.0% earnings per share growth, and the company has a 4.1% starting yield, which is offset by a potential valuation headwind. SWX earns a hold rating based on these factors.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | 1,951 | 2,122 | 2,464 | 2,460 | 2,549 | 2,880 | 3,120 | 3,299 | 3680 | 4960 |
| Gross Profit | 557 | 585 | 608 | 657 | 652 | 667 | 737 | 818 | 821 | 995 |
| Gross Margin | 28.5% | 27.6% | 24.7% | 26.7% | 25.6% | 23.1% | 23.6% | 24.8% | 22.3% | 20.1% |
| D&A Exp. | 237 | 253 | 270 | 289 | 251 | 249 | 303 | 332 | 371 | 470 |
| Operating Profit | 274 | 284 | 288 | 315 | 343 | 357 | 372 | 423 | 370 | 431 |
| Op. Margin | 14.1% | 13.4% | 11.7% | 12.8% | 13.5% | 12.4% | 11.9% | 12.8% | 10.0% | 8.7% |
| Net Profit | 145 | 141 | 138 | 152 | 194 | 182 | 214 | 232 | 201 | -203 |
| Net Margin | 7.4% | 6.7% | 5.6% | 6.2% | 7.6% | 6.3% | 6.9% | 7.0% | 5.5% | -4.1% |
| Free Cash Flow | (18) | (50) | 64 | 71 | (254) | (237) | (438) | (199) | -604 | -452 |
| Income Taxes | 78 | 78 | 80 | 78 | 65 | 62 | 56 | 66 | 40 | -76 |

Balance Sheet Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|-------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|--------|-------|
| Total Assets | 4,565 | 5,208 | 5,359 | 5,581 | 6,237 | 7,358 | 8,170 | 8,736 | 12,765 | 13197 |
| Cash & Equivalents | 41 | 40 | 36 | 28 | 44 | 85 | 50 | 83 | 223 | 123 |
| Goodwill & Int. | 18 | 191 | 163 | 178 | 179 | 359 | 343 | 345 | 1,781 | 787 |
| Total Liabilities | 3,153 | 3,722 | 3,766 | 3,920 | 4,425 | 5,106 | 5,664 | 6,061 | 9,811 | 9979 |
| Accounts Payable | 184 | 168 | 165 | 185 | 228 | 249 | 239 | 231 | 353 | 662 |
| Long-Term Debt | 1,392 | 1,656 | 1,589 | 1,600 | 2,038 | 2,292 | 2,675 | 2,880 | 6,322 | 5991 |
| Total Equity | 1,415 | 1,489 | 1,594 | 1,663 | 1,815 | 2,252 | 2,506 | 2,675 | 2,954 | 3059 |
| LTD/E Ratio | 0.98 | 1.11 | 1.00 | 0.96 | 1.12 | 1.02 | 1.07 | 1.08 | 2.14 | 1.96 |

Profitability & Per Share Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|-------------------------|--------|--------|-------|-------|--------|--------|--------|--------|--------|-------|
| Return on Assets | 3.2% | 2.9% | 2.6% | 2.8% | 3.3% | 2.7% | 2.8% | 2.7% | 1.9% | -1.6% |
| Return on Equity | 10.7% | 9.7% | 9.0% | 9.3% | 11.1% | 9.0% | 9.0% | 9.0% | 7.1% | -6.8% |
| ROIC | 5.4% | 4.7% | 4.4% | 4.7% | 5.5% | 4.3% | 4.4% | 4.3% | 2.7% | -2.2% |
| Shares Out. | 46.5 | 46.5 | 47.4 | 47.5 | 48.1 | 53.0 | 55.0 | 57.2 | 60.6 | 65.56 |
| Revenue/Share | 41.72 | 45.20 | 51.99 | 51.46 | 53.11 | 58.21 | 57.44 | 58.83 | 62.11 | 75.66 |
| FCF/Share | (0.39) | (1.08) | 1.35 | 1.48 | (5.29) | (4.79) | (8.06) | (3.55) | -10.20 | -6.89 |

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

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