

Atmos Energy Corp. (ATO)

\$97.33 (As of 05/08/20)

Price Target (6-12 Months): **\$102.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 05/04/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: C

Growth: C

Momentum: A

Summary

Atmos Energy's fiscal second-quarter earnings surpassed estimates but revenues lagged the same. The company reaffirmed the fiscal 2020 capital expenditure plan. High percentage of earnings from residential customers will assist the company to offset the decline in demand from other customer groups due to the novel coronavirus outbreak. Returns within one year of investment and positive regulatory outcomes will continue to boost the company's performance. Shares of Atmos Energy have outperformed the industry in the past 12 months. However, the mishap in the company's Northwest Dallas operation is a stark reminder of the fact that distributing and transporting natural gas involve risks. Dependence on a single state for bulk of its revenues exposes it to vagaries of weather, and economic conditions of that state.

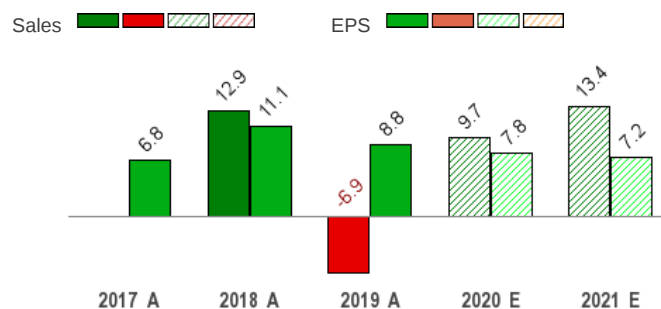
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$121.08 - \$77.92
20 Day Average Volume (sh)	797,804
Market Cap	\$11.9 B
YTD Price Change	-13.0%
Beta	0.33
Dividend / Div Yld	\$2.30 / 2.4%
Industry	Utility - Gas Distribution
Zacks Industry Rank	Top 9% (24 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.5%
Last Sales Surprise	-13.2%
EPS F1 Est- 4 week change	-0.2%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	21.2
P/E F1	20.8
PEG F1	3.2
P/S TTM	4.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,612 E
2020	876 A	978 A	529 E	488 E	3,184 E
2019	878 A	1,095 A	486 A	444 A	2,902 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.51 E	\$2.00 E	\$0.89 E	\$0.67 E	\$5.03 E
2020	\$1.47 A	\$1.95 A	\$0.77 E	\$0.54 E	\$4.69 E
2019	\$1.38 A	\$1.82 A	\$0.68 A	\$0.49 A	\$4.35 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/08/2020. The reports text is as of 05/11/2020.

Overview

Founded in 1906, Atmos Energy Corporation, along with its subsidiaries, is engaged in regulated natural gas distribution and storage business. The company serves in excess of three million natural gas distribution customers in more than 1,400 communities in eight states from the Blue Ridge Mountains in the East to the Rocky Mountains in the West. The company operates more than 75,000 miles of transmission and distribution lines.

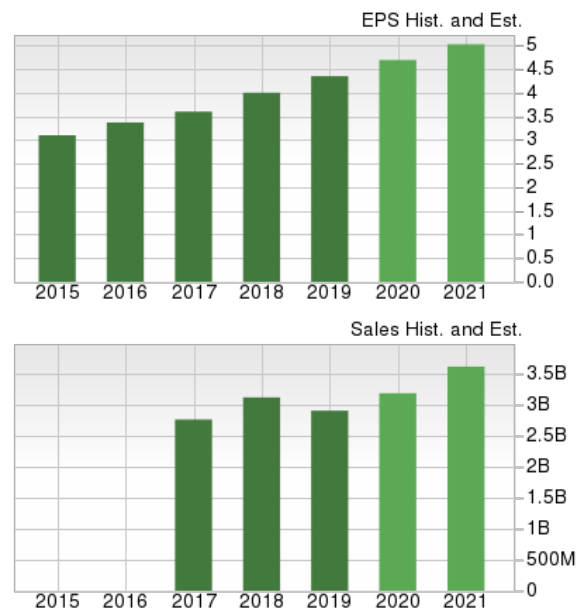
The company manages its operation through the following reportable segments.

Distribution segment is primarily comprised of the company's regulated natural gas distribution and related sales operations in eight states, and storage assets located in Kentucky and Tennessee. At the end of fiscal 2019, this segment contributed nearly \$2,745.5 million to its total revenues.

Pipeline and storage segment is primarily comprised of the pipeline and storage operations of Atmos Pipeline-Texas division, and the company's natural gas transmission operations in Louisiana. The company operates five storage facilities, having a combined storage capacity of 46 billion cubic feet. This segment contributed \$567.1 million to total fiscal 2019 revenues.

Inter-segment elimination had an adverse impact of \$410.7 million on fiscal 2019 revenues.

Till Dec 31, 2016, the company had a non-regulated natural gas marketing business that was conducted by Atmos Energy Marketing (AEM). However, effective Jan 1, 2017, it sold all of the equity interests of AEM to a subsidiary of CenterPoint Energy Inc. As a result of the sale, Atmos Energy fully exited from the non-regulated natural gas marketing business. Accordingly, these operations have been reported as discontinued operations.



Reasons To Buy:

- ▲ Atmos Energy has a sturdy capital expenditure plan, helping the company to increase safety and reliability of its natural gas pipelines. In fiscal 2019, the company invested \$1,693 million, out of which a major portion was utilized to improve the safety and reliability of distribution and transportation systems.

During the period fiscal 2015 to 2019 the company invested \$6.4 billion on replacing aging infrastructure and modernizing the system. In fiscal 2020, it intends to invest in the range of \$1,850-\$1,950 million to strengthen infrastructure. Out of the total, 85% will be spent on maintaining the safety and reliability of its services.

The company aims to replace up to 6,000 miles of old transmission and distribution lines over the next five years to make its systems more reliable. The company will replace all old cast iron pipelines by 2021, making its distribution system more reliable. The planned investment will result in 6-8% annual earnings growth over the same time frame. In the past 12 months, Atmos Energy's shares have lost 5.1%, narrower than the industry's 21.5% decline.

- ▲ The planned capital investment will allow Atmos Energy to lower emissions from its system. It aims at reducing methane emissions by 10-15% in the next five years from the current levels. The company also aims at lowering methane emissions by 50% within 2035.

It is carrying out investments for improving the quality of services. At present, nearly 59% of its revenues are generated from the residential customer group. The stay-at-home orders to control the spread of the novel coronavirus are expected to increase residential demand for gas, which in turn are likely to partly offset the decline in demand from other customer categories.

- ▲ More than 90% of Atmos Energy's annual capital investments start earning returns within six months and nearly 99% in no more than 12 months. Customers and investors gain from the constructive rate outcomes. Owing to positive regulatory outcome, \$115.2 million and \$58.2 million increase in rates has been implemented in fiscal 2019 and 2020 (till May 6, 2020), respectively. In addition, nearly \$215.8 million rate cases are in progress for implementation this fiscal year.

The company worked with regulators to ensure that utility customers receive full benefits of tax reform in their gas bills. Atmos Energy has agreed with the regulators and reduced customer bills, in order to reflect the lower statutory federal rate. Taking advantage of lower rates, the company reduced the weighted average cost of debt to 4.32% from 6.2% at end of fiscal 2014, which undoubtedly had a positive impact on margins.

- ▲ Consistent performance of the company has enabled it to reward its shareholders through consistent increase in annual dividend rates. The company has raised annual dividend for 36 consecutive years. Its board of directors has declared a quarterly dividend of 57.5 cents per common share. The new dividend for fiscal 2020 is \$2.30, which represents a 9.5% increase from fiscal 2019.

Given solid capital-expenditure plans, addition of customers and increase in consumption, it is expected that the company will continue with the annual dividend-increase policy over the long run.

- ▲ The long-term debt to capital of the company was 40.7% at the end of second-quarter fiscal 2020, which is lower than 41.1% at fiscal first-quarter 2020-end. The long-term debt to capital of the company is lower than the industry average of 51.1% and Zacks S&P 500 composite's 43.76%. At second quarter-end, cash and equivalents of the company were \$320 million, higher than the current debt level of \$200 million. It has been assigned top-tier credit ratings by rating agencies.

At second quarter-end, times interest earned ratio of the company was 8.3, which improved from 7.6 at the end of fiscal first-quarter 2020. This ratio is much better than the industry average of 2.79. The strong ratio indicates that the company will be able to meet current debt obligations without any difficulties. At a time when every entity is looking forward to preserve liquidity amid uncertainty as a result of the outbreak of COVID-19, the company's current times interest earned ratio is reassuring for investors.

Solid contribution from residential customers, returns within one year of investment, customer additions and positive regulatory outcomes will continue to boost the company's performance.

Reasons To Sell:

- ▼ Operations of the company are capital intensive, and despite making significant investment to upgrade and maintain infrastructure, there is always a possibility of accident and mishap. Sudden and unexplained leakage leading to three gas-related accidents in 1.5 square mile area of company's operation in Northwest Dallas is a reminder that despite undertaking precaution at the time of distributing, transporting and storing natural gas, there will be a possibility of mishap.
- ▼ Courtesy of regulated operations, it does not face direct competition from any other distributor of natural gas to residential and commercial customers within its service areas. However, the company has to compete with other suppliers of natural gas and alternative fuels for sales to industrial customers. In addition, the company has to compete with electric utilities like natural gas, as well as electricity used for space and water heating, and cooking market.
- ▼ Nearly 70% of Atmos Energy's consolidated operations are located in the State of Texas. Its operations and financial results are vulnerable to state economic conditions, weather patterns and regulatory decisions. More than 50% of the company's distribution customers and most of its pipeline and storage assets and operations are located in the State of Texas.

Competition from other fuel sources, dependence on a single state and the possibility of accident in gas pipelines are headwinds.

Last Earnings Report

Atmos Energy Q2 Earnings Beat Estimates, Revenues Miss

Atmos Energy Corporation posted second-quarter fiscal 2020 earnings of \$1.95 per share, which surpassed the Zacks Consensus Estimate by a penny.

The reported earnings also improved 7.1% from the prior-year figure. The year-over-year improvement in earnings was due to positive rate outcomes and customer growth in the distribution segment.

Quarter Ending 03/2020

Report Date	May 06, 2020
Sales Surprise	-13.24%
EPS Surprise	0.52%
Quarterly EPS	1.95
Annual EPS (TTM)	4.59

Total Revenues

Total revenues of \$978 million missed the Zacks Consensus Estimate of \$1,127 million by 13.2% and decreased 10.6% from the year-ago figure of \$1,094.7 million.

Segment Revenues

Distribution: Revenues from the segment decreased 11.8% to \$933 million from \$1,057.9 million in the prior-year quarter.

Pipeline and Storage: Revenues from the segment increased 7.8% to \$146.2 million from \$135.7 million in the year-ago quarter. The improvement was driven by an increase in rates, marginally offset by a rise in depreciation expenses.

Quarterly Highlights

Purchased gas cost in the quarter was \$317.9 million, down 32.6% from the year-ago period. Operation and maintenance expense in the quarter was \$147.8 million, down 1.1% from the year-ago period.

Operating income in the reported quarter was up 11.3% year over year to \$331.5 million.

The company incurred interest expenses of \$22.2 million, down 17.5% from the year-ago period.

Financial Highlights

As of Mar 31, 2020, Atmos Energy had cash and cash equivalents of \$320.1 million compared with \$24.6 million on Sep 30, 2019.

Long-term debt was \$4.3 billion as of Mar 31, 2020, up from \$3.53 billion on Sep 30, 2019.

The company's cash flow from operating activities in the first six months of fiscal 2020 was \$633.8 million, up from \$520.8 million recorded in the year-ago period.

It invested \$994.7 million in the first six months of fiscal 2020 compared with \$777.6 million in the comparable year-ago period. The increase in capital spending was due to continued spending for infrastructure replacements and enhancements.

Guidance

Since the impact of the novel coronavirus remains uncertain, Atmos Energy reiterated its fiscal 2020 earnings guidance in the range of \$4.58-\$4.73 per share. The Zacks Consensus Estimate for fiscal 2020 earnings is \$4.69 per share. Capital expenditure view also remains unchanged and is expected in the range of \$1.85-\$1.95 billion for fiscal 2020.

Valuation

Atmos Energy shares are down 13% in the year- to-date period, and 5.1% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utility sector are down 26.6% and 16.6% in the year- to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 21.5% and 20.4% respectively.

The S&P 500 index is down 9% in the year- to-date period but up 4% in the past year.

The stock is currently trading at 19.88X of forward 12 months earnings, which compares to 14.56X for the Zacks sub-industry, 11.9X for the Zacks sector and 21.15X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.07X and as low as 16.25X, with a 5-year median of 21.75X. Our Neutral recommendation indicates that the stock will perform inline with the market. Our \$102 price target reflects 20.85X of forward 12 months earnings.

The table below shows summary valuation data for ATO

Valuation Multiples - ATO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	19.88	14.56	11.9	21.15
	5-Year High	26.07	23.03	15.32	21.15
	5-Year Low	16.25	12.59	11.38	15.19
	5-Year Median	21.75	20.39	13.78	17.45
P/S F 12M	Current	3.46	1.69	2.54	3.3
	5-Year High	4.24	2.3	3.29	3.44
	5-Year Low	0.93	1.02	1.75	2.54
	5-Year Median	2.79	1.67	2.04	3.02
P/B TTM	Current	1.89	1.41	3.14	3.85
	5-Year High	2.51	2.68	4.05	4.55
	5-Year Low	1.6	1.18	2.01	2.84
	5-Year Median	2.19	2.21	2.6	3.64

As of 05/08/2020

Industry Analysis Zacks Industry Rank: Top 9% (24 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
National Fuel Gas Company (NFG)	Outperform	1
CenterPoint Energy Inc (CNP)	Neutral	3
MDU Resources Group Inc (MDU)	Neutral	3
NewJersey Resources Corporation (NJR)	Neutral	3
ONE Gas Inc (OGS)	Neutral	2
Spire Inc (SR)	Neutral	3
Southwest Gas Corporation (SWX)	Neutral	3
UGI Corporation (UGI)	Neutral	3

Industry Comparison Industry: Utility - Gas Distribution				Industry Peers		
	ATO	X Industry	S&P 500	MDU	NJR	SWX
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	C	F	B
Market Cap	11.90 B	3.97 B	20.19 B	4.39 B	3.37 B	4.19 B
# of Analysts	4	2	14	1	2	3
Dividend Yield	2.36%	3.36%	2.12%	3.79%	3.54%	2.87%
Value Score	C	-	-	C	D	C
Cash/Price	0.02	0.01	0.06	0.02	0.00	0.01
EV/EBITDA	13.90	11.18	11.95	8.80	19.06	11.18
PEG Ratio	3.19	2.77	2.60	2.74	2.79	3.39
Price/Book (P/B)	1.89	1.74	2.75	1.54	1.74	1.66
Price/Cash Flow (P/CF)	12.61	9.15	10.78	7.42	11.91	8.03
P/E (F1)	20.75	18.05	19.85	13.68	16.74	20.35
Price/Sales (P/S)	4.28	1.65	2.03	0.81	1.56	1.34
Earnings Yield	4.82%	5.54%	4.83%	7.31%	5.98%	4.92%
Debt/Equity	0.69	1.02	0.75	0.81	0.84	0.92
Cash Flow (\$/share)	7.72	3.61	7.01	2.95	2.96	9.47
Growth Score	C	-	-	D	F	B
Hist. EPS Growth (3-5 yrs)	9.11%	6.69%	10.87%	10.39%	5.31%	7.66%
Proj. EPS Growth (F1/F0)	7.87%	2.07%	-9.87%	-5.33%	8.21%	-5.16%
Curr. Cash Flow Growth	12.19%	10.67%	5.88%	20.75%	-18.24%	19.86%
Hist. Cash Flow Growth (3-5 yrs)	11.14%	7.61%	8.55%	7.61%	3.04%	5.91%
Current Ratio	0.89	0.81	1.24	1.50	0.86	0.80
Debt/Capital	40.71%	48.76%	44.23%	44.79%	45.69%	48.76%
Net Margin	20.02%	8.18%	10.68%	6.28%	7.21%	6.86%
Return on Equity	9.35%	9.09%	16.36%	12.29%	9.89%	8.83%
Sales/Assets	0.20	0.29	0.55	0.70	0.54	0.40
Proj. Sales Growth (F1/F0)	9.71%	0.00%	-2.26%	0.00%	-3.01%	5.09%
Momentum Score	A	-	-	A	B	A
Daily Price Chg	0.99%	3.12%	2.40%	4.44%	5.43%	5.45%
1 Week Price Chg	-4.13%	-1.73%	0.53%	-5.16%	1.89%	-5.25%
4 Week Price Chg	-7.48%	-0.49%	2.68%	-11.34%	-1.26%	-2.76%
12 Week Price Chg	-18.55%	-17.55%	-19.20%	-30.82%	-18.09%	-4.88%
52 Week Price Chg	-3.35%	-19.22%	-8.44%	-14.70%	-27.78%	-4.45%
20 Day Average Volume	797,804	465,970	2,398,409	1,121,256	563,031	498,584
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.16%	0.00%	-6.95%	0.00%	0.96%	0.72%
(F1) EPS Est 12 week change	0.05%	-1.72%	-15.68%	-8.57%	-1.86%	-4.35%
(Q1) EPS Est Mthly Chg	-1.28%	-4.23%	-13.12%	NA	0.00%	-17.14%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	C
Momentum Score	A
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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