

Atmos Energy Corp. (ATO)

\$98.98 (As of 08/27/20)

Price Target (6-12 Months): **\$104.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/27/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: D

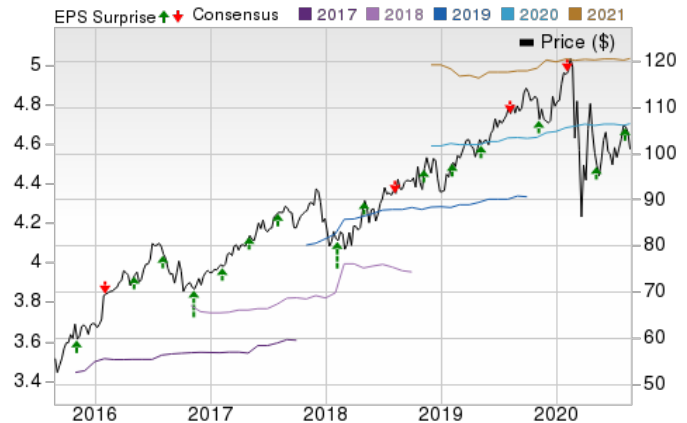
Growth: C

Momentum: D

Summary

Atmos Energy's fiscal third-quarter earnings beat estimates but revenues miss the same. Higher contribution from residential customers will assist the company to offset the decline in demand from other customer groups due to the pandemic. Its long-term capital spending plan will strengthen operations. Returns within one year of investment will continue to boost the company's performance. Steady performance allows the company to pay dividend at regular intervals. Shares of Atmos Energy have outperformed the industry in the past three 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.

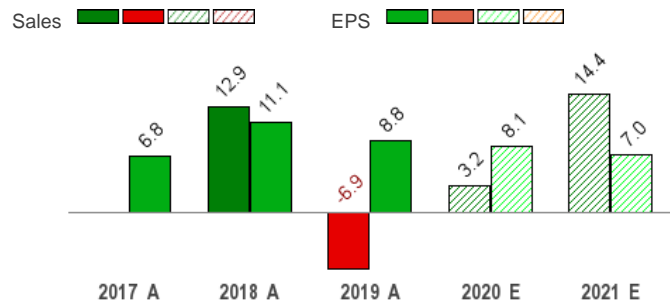
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$121.08 - \$77.92
20 Day Average Volume (sh)	831,729
Market Cap	\$12.2 B
YTD Price Change	-11.5%
Beta	0.31
Dividend / Div Yld	\$2.30 / 2.3%
Industry	Utility - Gas Distribution
Zacks Industry Rank	Bottom 34% (167 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.0%
Last Sales Surprise	-20.6%
EPS F1 Est- 4 week change	0.2%
Expected Report Date	11/04/2020
Earnings ESP	0.5%
P/E TTM	21.1
P/E F1	21.1
PEG F1	3.2
P/S TTM	4.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,427 E
2020	876 A	978 A	493 A	570 E	2,996 E
2019	878 A	1,095 A	486 A	444 A	2,902 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.55 E	\$2.05 E	\$0.84 E	\$0.61 E	\$5.03 E
2020	\$1.47 A	\$1.95 A	\$0.79 A	\$0.52 E	\$4.70 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 08/27/2020. The reports text is as of 08/28/2020.

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 72,000 miles of transmission and distribution lines, as well as 5,700 miles of interstate pipelines.

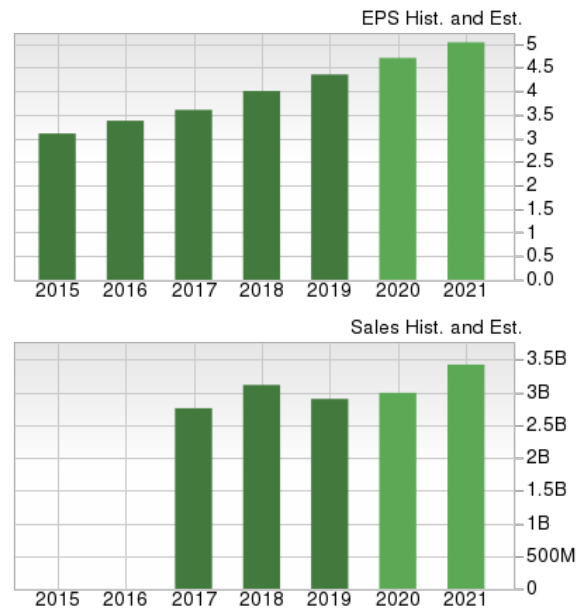
The company manages its operation through the following reportable segments.

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.

The company is planning to invest in the range of \$10-\$11 billion from fiscal 2020 through 2024, out of which 85% will be allocated to enhance the safety of the existing operations. The planned investment will result in 6-8% annual earnings growth over the same time frame.

Maintenance and upgrade of the existing infrastructure is of utmost importance to the company. Atmos Energy 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, which will make the distribution system more reliable. It is also replacing 30,000-40,000 steel service lines annually to safeguard against 70% gas leaks occurring in service lines. In the past three months, Atmos Energy's shares have lost 3.7%, narrower than the industry's 8.8% 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 57% 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, operating income of Atmos Energy in the first nine months of fiscal 2020 improved \$110.8 million from the year-ago period. In addition, nearly \$140.5 million rate cases are in progress for implementation this fiscal year.
- ▲ 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. The company aims to increase dividend in the range of 6-8% per year, subject to approval of the board of directors. 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 company's long-term debt to capital was 41.2% at the end of third-quarter fiscal 2020, lower than 41.4% at fiscal first-quarter 2020-end. Its long-term debt to capital is also lower than the industry average of 56.4% and Zacks S&P 500 composite's 49.76%. It has been assigned top-tier credit ratings by rating agencies. As of Jun 30, 2020, the company had \$2.9 billion available liquidity, which was enough to meet the current obligations. Apart from 2.29% notes worth \$200 million due 2022, the company does not have any substantial debt maturity till 2027, when \$500 million of notes with coupon rate of 3% are set to mature.

At fiscal third quarter-end, times interest earned ratio of the company was 8.5, which improved from 7.6 at the end of fiscal first-quarter 2020. This ratio is much better than the industry average of 2.68. The strong ratio indicates that the company will be able to meet the current debt obligations without any difficulty. At a time when every entity is looking forward to preserve liquidity amid uncertainty as a result of the COVID-19 outbreak, its 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 Q3 Earnings Beat Estimates, Revenues Miss

Atmos Energy Corporation posted third-quarter fiscal 2020 earnings of 79 cents per share, which surpassed the Zacks Consensus Estimate of 76 cents by 3.9%.

The reported earnings also improved 16.2% from the prior-year figure. The year-over-year improvement in earnings was due to positive rate outcomes in both the segments, and lower operation and maintenance expenses in the distribution segment.

Quarter Ending 06/2020

Report Date	Aug 05, 2020
Sales Surprise	-20.55%
EPS Surprise	3.95%
Quarterly EPS	0.79
Annual EPS (TTM)	4.70

Total Revenues

Total revenues of \$492.9 million missed the Zacks Consensus Estimate of \$621 million by 20.6%. However, the top line increased 1.5% from the year-ago figure of \$485.8 million.

Segment Revenues

Distribution: Revenues from the segment decreased 2.2% to \$435.3 million from \$444.9 million in the prior-year quarter.

Pipeline and Storage: Revenues from the segment increased 5.9% to \$158 million from \$149.2 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 \$26.1 million, down 16.6% from the year-ago period. Operation and maintenance expenses for the quarter were \$149.5 million, down 9.1% from the year-ago period.

Operating income for the reported quarter was up 13.8% year over year to \$139.1 million.

The company incurred interest expenses of \$19.6 million, on par with the year-ago period.

Financial Highlights

As of Jun 30, 2020, Atmos Energy had cash and cash equivalents of \$208.6 million compared with \$24.6 million on Sep 30, 2019.

Long-term debt was \$4.53 billion as of Jun 30, 2020, up from \$3.53 billion on Sep 30, 2019.

The company's cash flow from operating activities for the first nine months of fiscal 2020 was \$895.5 million, up from \$808.9 million recorded in the comparable year-ago period.

It invested \$1,405.7 million in the first nine months of fiscal 2020 to strengthen operations. The figure was up 17% from the year-ago period. Nearly 88% of the capital spending was related to system safety and increased reliability of its services.

Guidance

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 11.5% in the year- to-date period, and down 8.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utility sector are down 29.9% and 15% in the year- to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 26.5% and 11.4% respectively.

The S&P 500 index is up 8.2% in the year- to-date period and up 19.5% in the past year.

The stock is currently trading at 19.79X of forward 12 months earnings, which compares to 13.77X for the Zacks sub-industry, 12.48X for the Zacks sector and 23.37X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.07X and as low as 16.33X, with a 5-year median of 21.75X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$104 price target reflects 20.8X 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 F12M	Current	19.79	13.77	12.48	23.37
	5-Year High	26.07	23.03	15.28	23.37
	5-Year Low	16.33	12.59	11.3	15.25
	5-Year Median	21.75	20.39	13.72	17.58
P/S F12M	Current	3.6	1.71	2.65	3.82
	5-Year High	4.24	2.3	3.29	3.82
	5-Year Low	0.95	1.02	1.75	2.53
	5-Year Median	2.84	1.69	2.07	3.05
P/B TTM	Current	1.87	1.6	4.14	4.71
	5-Year High	2.51	2.68	4.29	4.71
	5-Year Low	1.61	1.41	2.01	2.83
	5-Year Median	2.19	2.21	2.64	3.76

As of 8/27/2020

Industry Analysis Zacks Industry Rank: Bottom 34% (167 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
CenterPoint Energy, Inc. (CNP)	Neutral	3
MDU Resources Group, Inc. (MDU)	Neutral	3
National Fuel Gas Company (NFG)	Neutral	3
ONE Gas, Inc. (OGS)	Neutral	4
Spire Inc. (SR)	Neutral	3
Southwest Gas Corporation (SWX)	Neutral	3
UGI Corporation (UGI)	Neutral	2
NewJersey Resources Corporation (NJR)	Underperform	3

Industry Comparison Industry: Utility - Gas Distribution				Industry Peers		
	ATO	X Industry	S&P 500	MDU	NJR	SWX
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	D	-	-	B	D	B
Market Cap	12.21 B	3.68 B	23.67 B	4.71 B	2.87 B	3.46 B
# of Analysts	5	3	14	1	2	1
Dividend Yield	2.32%	3.53%	1.64%	3.53%	4.17%	3.69%
Value Score	D	-	-	B	C	B
Cash/Price	0.02	0.07	0.07	0.01	0.01	0.05
EV/EBITDA	14.32	10.36	13.33	9.29	17.50	10.24
PEG Ratio	3.22	2.94	3.05	2.94	2.41	3.36
Price/Book (P/B)	1.87	1.70	3.18	1.63	1.56	1.31
Price/Cash Flow (P/CF)	12.82	8.34	12.81	7.97	10.11	6.53
P/E (F1)	20.95	16.04	21.68	14.69	14.47	16.80
Price/Sales (P/S)	4.38	1.61	2.50	0.86	1.41	1.09
Earnings Yield	4.75%	6.19%	4.43%	6.81%	6.91%	5.95%
Debt/Equity	0.70	0.97	0.74	0.81	0.91	1.01
Cash Flow (\$/share)	7.72	4.07	6.94	2.95	2.96	9.47
Growth Score	C	-	-	A	D	C
Hist. EPS Growth (3-5 yrs)	9.06%	7.73%	10.41%	13.22%	2.60%	7.73%
Proj. EPS Growth (F1/F0)	8.09%	1.18%	-4.94%	-5.33%	6.15%	-6.60%
Curr. Cash Flow Growth	12.19%	10.67%	5.22%	20.75%	-18.24%	19.86%
Hist. Cash Flow Growth (3-5 yrs)	11.14%	8.55%	8.50%	7.61%	3.04%	5.91%
Current Ratio	0.86	0.79	1.35	1.40	0.58	0.94
Debt/Capital	41.22%	49.25%	43.86%	44.78%	47.51%	51.08%
Net Margin	21.31%	7.55%	10.25%	6.50%	8.30%	6.55%
Return on Equity	9.31%	9.37%	14.66%	12.52%	9.43%	8.84%
Sales/Assets	0.19	0.27	0.50	0.71	0.41	0.39
Proj. Sales Growth (F1/F0)	3.23%	-1.09%	-1.43%	0.00%	-20.33%	3.72%
Momentum Score	D	-	-	F	A	D
Daily Price Chg	-0.32%	0.00%	0.43%	2.44%	-0.17%	-0.34%
1 Week Price Chg	-3.50%	-2.75%	-1.45%	-2.61%	-4.85%	-7.56%
4 Week Price Chg	-6.11%	-3.84%	3.75%	10.17%	-4.53%	-11.50%
12 Week Price Chg	-5.03%	-8.21%	3.95%	5.38%	-14.01%	-16.15%
52 Week Price Chg	-10.00%	-27.69%	2.75%	-12.35%	-34.07%	-31.54%
20 Day Average Volume	831,729	308,115	1,887,168	1,175,013	498,101	282,868
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	-0.69%
(F1) EPS Est 4 week change	0.17%	0.09%	0.79%	0.00%	-1.43%	0.61%
(F1) EPS Est 12 week change	0.04%	-0.11%	3.43%	0.00%	-1.43%	2.35%
(Q1) EPS Est Mthly Chg	-2.03%	-2.94%	0.00%	NA	25.00%	-51.28%

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	D
Growth Score	C
Momentum Score	D
VGM Score	D

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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