

ONE Gas, Inc. (OGS)

\$77.03 (As of 03/15/21)

Price Target (6-12 Months): **\$81.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 12/16/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: C

Growth: F

Momentum: D

Summary

ONE Gas is gaining from residential customer growth, which in turn is boosting demand for natural gas and driving its performance. The company will benefit from investment that is aimed at strengthening its infrastructure and systems integrity. The company's 100% regulated operation and high percentage of residential customers increase earnings visibility. The company manages its debts quite efficiently and strengthens its balance sheet. However, in the past year, One Gas' shares have underperformed the industry. Seasonality of the business, a highly-competitive industry and competition from other sources of energy used for heating are the primary headwinds. Any failure to meet the stringent regulations can affect the company's operations or financial results.

Price, Consensus & Surprise

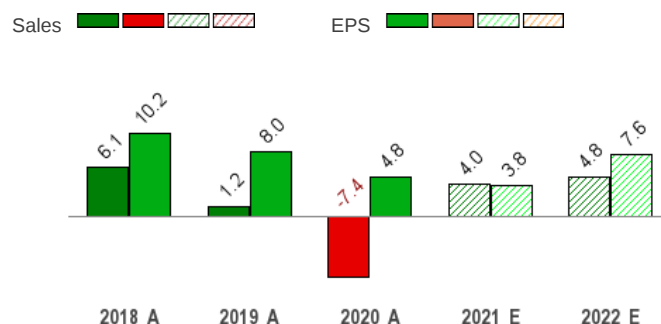


Source: Zacks Investment Research

Data Overview

52-Week High-Low	\$92.00 - \$63.67
20-Day Average Volume (Shares)	324,857
Market Cap	\$4.0 B
Year-To-Date Price Change	-2.1%
Beta	0.40
Dividend / Dividend Yield	\$2.32 / 3.0%
Industry	Utility - Gas Distribution
Zacks Industry Rank	Top 45% (115 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	2.8%
Last Sales Surprise	5.1%
EPS F1 Estimate 4-Week Change	-0.2%
Expected Report Date	04/26/2021
Earnings ESP	-0.7%
P/E TTM	20.4
P/E F1	20.2
PEG F1	3.5
P/S TTM	2.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022					1,668 E
2021	544 E	293 E	266 E	513 E	1,591 E
2020	528 A	273 A	245 A	484 A	1,530 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022					\$4.11 E
2021	\$1.80 E	\$0.50 E	\$0.46 E	\$1.09 E	\$3.82 E
2020	\$1.72 A	\$0.48 A	\$0.39 A	\$1.09 A	\$3.68 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 03/15/2021. The report's text and the analyst-provided price target are as of 03/16/2021.

Overview

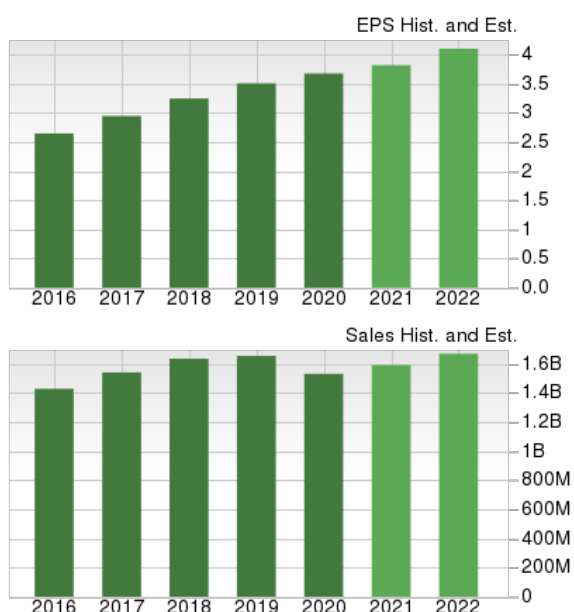
Headquartered in Tulsa, OK, ONE Gas, Inc. is a 100% regulated natural gas distribution utility. The company provides natural gas distribution services to more than 2.2 million customers in Oklahoma, Kansas and Texas. The company has been registering an increase in average customer count in these three states since 2014. AAs of Dec 31, 2020, it operated 43,700 miles of natural gas distribution and transmission pipelines.

ONE Gas is the successor to the company founded in 1906 as Oklahoma Natural Gas Company, which became ONEOK, Inc. in 1980. On Jan 31, 2014, ONE Gas officially separated from ONEOK.

The company operates through three divisions, namely Oklahoma Natural Gas, Kansas Gas Service and Texas Gas Service. For the year ended Dec 31, 2020, nearly 87%, 55% and 70% of net margin from sales customers was recovered from fixed charges for Oklahoma Natural Gas, Kansas Gas Service, and Texas Gas Service, respectively. As of Dec 31, 2020, it had 48.3 billion cubic feet (Bcf) of natural gas storage capacity under contract. The term of the contracts ranges from one to ten years.

ONE Gas' business strategy is focused on operating its systems in a safe, reliable and environmentally responsible manner, and strategically growing business, while delivering good quality customer service. ONE Gas' existing assets have close a proximity to significant natural gas reserves and transportation infrastructure. This results in lower transportation, storage and commodity costs, thereby giving the company a competitive advantage over peers.

The company operates through one reportable and operating business segment, namely regulated public utilities that deliver natural gas to residential, commercial, industrial and transportation customers.



Source: Zacks Investment Research

Reasons To Buy:

- ▲ After investing \$470 million in 2019, ONE Gas invested \$515 million in 2020 and plans to invest \$540 million in 2021. The increase is primarily driven by the extension of services to new customers. The ongoing capital expenditures are directed toward pipeline integrity, extension of services to new areas, increase in system capacity, pipeline replacements, automated meter reading, government-mandated pipeline relocations, facilities, information technology assets and cybersecurity.

The company now aims to invest nearly \$3 billion over the 2021 to 2024 time period. Nearly 65-70% of the planned capital expenditure will be directed toward systems integrity and replacement projects. It continues to make progress in the Vintage Pipeline Replacement Program. One Gas has been replacing vintage pipelines at a rate of 234 miles per year over the past five years. This replacement program will continue for the next couple of decades to complete the upgrade of all vintage lines.

- ▲ ONE Gas is managing its long-term debt quite efficiently and working toward consistently lowering the same. Its debt to capital has been declining over the past few years. At the end of fourth-quarter 2020, the company's total debt to capital was 41.4%, which compares favorably with the industry average of 49.4%. It has top-tier credit rating and its outlook is stable.

The company's times interest earned ratio at the end of fourth-quarter 2020 was 4.8, up 10 basis points sequentially. A strong ratio indicates that the company will be able to meet debt obligations in the near future without any difficulties. At a time when every entity is looking forward to preserving liquidity amid uncertainty as a result of the outbreak of COVID-19, this stable ratio is reassuring for investors.

- ▲ Regular investment in a fully-regulated company and its ability to generate sufficient cash flows will support management's plans of rewarding shareholders through average annual dividend increase of 6-8% in the 2019-2024 time period. The targeted dividend payout ratio of the company is 55-65% of net income, subject to approval of the board of directors.

Courtesy of its stable performance, the company is raising annual dividend for the past few years. The 2021 annual dividend of \$2.32 per shares reflects an increase of 38.1% from the 2017 level and 7.4% from 2020.

- ▲ This 100% regulated natural gas distribution utility has a high percentage of residential customers, providing stability and strong visibility of forward earnings. The company was able to register higher customer additions in 2020 than 2019 levels. One Gas is expected to continue with customer additions in 2021 as well, courtesy of improving economic conditions in its service territories. The company is steadily increasing the customer base every year from 2015 base. The majority of the total customer base comprises residential customers. During 2020, nearly 72% of net sales margin was attributed to residential customers. The company continues to supply natural gas to a large group of customers. This in a way provides stability to the company's earnings, as the loss of any customer will not substantially affect One Gas' top line.

The new rates effective in Oklahoma, Kansas and Texas will continue to boost annual revenues of the company. Systematic expenditure and rate approval from the commission will enable it to continue with infrastructure strengthening initiatives. In addition, ONE Gas' supply assets are in close proximity to gas reserves. This results in lower transportation, storage and commodity costs, as well as provides it with a competitive advantage.

Regulated earnings, stable debt profile, steady demand from residential customers, new rates and systematic capital expenditure will drive the company's performance.

Reasons To Sell:

- ▼ The company depends on natural gas distribution for its earnings. However, restrictions or regulations on shale natural gas production and waste water disposal could result in an upward movement in the prices of natural gas, which might in turn lead to migration of customers to alternative cheaper sources of fuel, thereby impacting business and financial conditions. In the past 12-month period, shares of One Gas have lost 9%, against the industry's 29.1% rally.

The company provides natural gas distribution services to customers in Oklahoma, Kansas and Texas. Any changes in regional economies and weather patterns of these states could adversely impact growth opportunities, usage patterns and financial condition of customers, in turn adversely impacting profitability. Due to late payment, reconnect and collection fees —primarily related to the moratoriums on disconnects for nonpayment in response to the COVID-19 pandemic — resulted in a \$2.4-million decline in operating income for the fourth quarter.

- ▼ The natural gas industry is highly competitive and the company has to compete against a large number of competitors to retain customers and prove reliability of its services. Natural gas competes with electricity for water, space heating and other energy-related needs. A fall in the price of electricity or other energy products will make natural gas less attractive to customers and hence reduce its demand, hurting prospects of the company.
- ▼ Natural gas sales to residential and commercial customers are seasonal, as a substantial portion of their natural gas requirements are for heating. Accordingly, the demand of natural gas is higher normally during the months of November through March than in other months of the year. If winter weather is warmer it would have an adverse impact on demand and profitability of the company.
- ▼ The company is subject to laws, regulations and other legal requirements enacted or adopted by federal, state and local governmental authorities relating to environmental, health, and safety matters. Any failure to comply with these regulations could result in significant fines or penalties and adversely affect its operations or financial results.

Competition with other clean energy sources, low commodity prices, stringent regulations and seasonality of business are headwinds for the company.

Last Earnings Report

ONE Gas Beats Q4 Earnings Estimates, Adds Customers

ONE Gas Inc. reported fourth-quarter 2020 earnings of \$1.09 per share, beating the Zacks Consensus Estimate of \$1.06 by 2.8%.

The bottom line also improved 13.5% from the year-ago earnings, primarily owing to new rates, higher sales volumes in Kansas and Oklahoma, along with residential customer growth.

Total Revenues

The company recorded revenues of \$484.2 million for the fourth quarter, which surpassed the Zacks Consensus Estimate of \$461 million by 5.1%. The top line also improved 6.9% from the year-ago level.

Quarterly Highlights

Residential natural gas sales volume for the fourth quarter was 42.9 billion cubic feet (Bcf), up 2.6% year over year. Total volumes delivered in the same period were 113.8 Bcf, down 0.5% from the year-ago period due to lower commercial and industrial sales volume.

Total operating expenses for the reported quarter increased 6.1% from the year-ago figure to \$190.9 million.

Operating income for the reported quarter improved 3.9% year over year to \$85.1 million.

For fourth-quarter 2020, ONE Gas' customer base rose 1.4% from the year-ago period, primarily due to additions to the residential customer group.

It incurred net interest expenses of \$15.4 million, down 1.9% from the prior-year figure.

Capital expenditures and asset removal costs were \$134.3 million for the reported quarter compared with \$121.2 million in the year-ago period, primarily due to increased system integrity activities and extension of services to new areas.

Financial Highlights

As of Dec 31, 2020, ONE Gas had cash and cash equivalents of \$8 million compared with \$17.9 million at 2019-end.

Long-term debt (excluding current maturities) was \$1,582.2 million as of Dec 31, 2020 compared with \$1,286.1 million in the corresponding period of 2019.

Cash provided by operating activities for 2020 was \$364.5 million compared with \$310.3 million in 2019.

Guidance

ONE Gas reaffirmed 2021 net income guided range of \$198-\$210 million and earnings per share expectation in the \$3.68-\$3.92 band. The midpoint of its EPS guidance is \$3.80, lower than the current Zacks Consensus Estimate of \$3.83 for the period.

Capital expenditure is expected to be \$540 million for 2021, with more than 70% of the amount targeted for system integrity and the balance primarily for customer growth.

Quarter Ending 12/2020

Report Date	Feb 25, 2021
Sales Surprise	5.11%
EPS Surprise	2.83%
Quarterly EPS	1.09
Annual EPS (TTM)	3.68

Valuation

ONE Gas shares are up 0.5% in the year-to-date period, and down 9% over the trailing 12-month period. Stocks in the Zacks sub-industry was up 13.5% and the Zacks Utility sector was up 1.1% in the year-to-date period. Over the past year, the Zacks sub-industry was up 29.1% and the sector was up 12.8%.

The S&P 500 index is up 6% in the year-to-date period but up 59.2% in the past year.

The stock is currently trading at 19.85X of forward 12 months earnings, which compares to 16.51X for the Zacks sub-industry, 13.64X for the Zacks sector and 22.59X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.8X and as low as 17.29X, with a 5-year median of 23.26X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$81 price target reflects 20.87X of forward 12 months earnings.

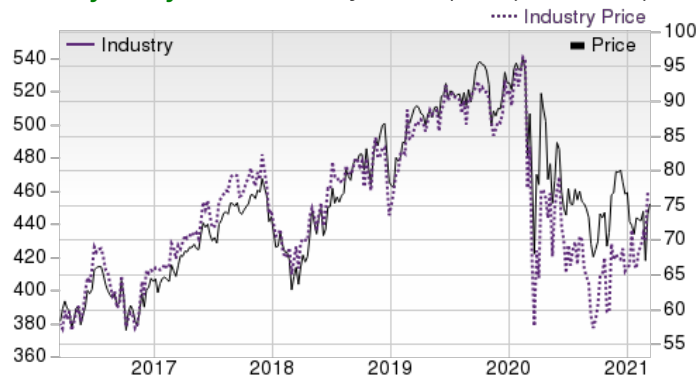
The table below shows summary valuation data for OGS

Valuation Multiples - OGS					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	19.85	16.51	13.64	22.59
	5-Year High	26.8	23.03	15.39	23.8
	5-Year Low	17.29	13.41	11.39	15.3
	5-Year Median	23.36	20.39	13.89	17.9
P/S F12M	Current	2.55	2.12	2.73	4.59
	5-Year High	2.96	2.35	3.2	4.59
	5-Year Low	1.7	1.36	1.79	3.21
	5-Year Median	2.47	1.81	2.17	3.69
P/B TTM	Current	1.83	2.02	2.97	6.7
	5-Year High	2.41	2.7	3.87	6.7
	5-Year Low	1.59	1.4	2.26	3.83
	5-Year Median	1.91	2.26	2.61	4.97

As of 3/15/2021

Source: Zacks Investment Research

Industry Analysis Zacks Industry Rank: Top 45% (115 out of 253)



Source: Zacks Investment Research

Top Peers

Company (Ticker)	Rec	Rank
Atmos Energy Corporation (ATO)	Neutral	3
National Fuel Gas Company (NFG)	Neutral	3
NewJersey Resources Corporation (NJR)	Neutral	2
Northwest Natural Gas Company (NWN)	Neutral	3
ONEOK, Inc. (OKE)	Neutral	3
South Jersey Industries, Inc. (SJI)	Neutral	3
Spire Inc. (SR)	Neutral	3
Sempra Energy (SRE)	Neutral	3

The positions listed should not be deemed a recommendation to buy, hold or sell.

Industry Comparison Industry: Utility - Gas Distribution				Industry Peers		
	OGS	X Industry	S&P 500	NFG	SJI	SR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	D	-	-	A	C	D
Market Cap	4.00 B	4.10 B	28.65 B	4.53 B	2.81 B	3.88 B
# of Analysts	4	2	13	2	5	5
Dividend Yield	3.09%	2.85%	1.38%	3.58%	4.33%	3.46%
Value Score	C	-	-	B	B	C
Cash/Price	0.00	0.02	0.06	0.02	0.01	0.00
EV/EBITDA	11.46	12.20	16.24	20.65	12.20	16.38
PEG F1	3.45	2.86	2.38	NA	0.67	3.66
P/B	1.79	1.97	3.92	2.22	1.69	1.66
P/CF	10.45	9.53	16.36	8.05	8.63	9.49
P/E F1	20.15	16.64	21.26	13.22	16.31	18.31
P/S TTM	2.61	2.22	3.30	2.94	1.82	2.16
Earnings Yield	5.08%	6.01%	4.59%	7.56%	6.12%	5.46%
Debt/Equity	0.71	1.01	0.67	1.04	1.67	1.07
Cash Flow (\$/share)	7.37	3.37	6.78	6.20	3.32	7.87
Growth Score	F	-	-	B	F	D
Historical EPS Growth (3-5 Years)	8.71%	7.65%	9.32%	0.69%	NA	2.01%
Projected EPS Growth (F1/F0)	3.87%	8.50%	14.55%	28.77%	1.90%	9.15%
Current Cash Flow Growth	6.58%	9.04%	0.72%	-1.88%	41.12%	7.51%
Historical Cash Flow Growth (3-5 Years)	9.20%	9.44%	7.32%	-0.85%	11.92%	8.52%
Current Ratio	0.68	0.87	1.39	0.50	0.44	0.50
Debt/Capital	41.47%	49.38%	41.42%	51.03%	62.49%	49.38%
Net Margin	12.84%	9.21%	10.59%	-8.59%	10.19%	6.12%
Return on Equity	8.91%	9.77%	14.65%	12.86%	10.06%	9.09%
Sales/Assets	0.26	0.26	0.51	0.22	0.24	0.22
Projected Sales Growth (F1/F0)	3.95%	3.95%	6.95%	28.16%	-2.29%	-0.51%
Momentum Score	D	-	-	A	A	C
Daily Price Change	2.53%	1.39%	0.92%	0.38%	2.54%	-0.65%
1-Week Price Change	2.08%	2.71%	2.96%	1.35%	4.69%	5.94%
4-Week Price Change	5.97%	6.57%	4.69%	13.44%	21.05%	16.68%
12-Week Price Change	1.78%	18.17%	10.09%	20.18%	36.32%	21.90%
52-Week Price Change	11.04%	31.62%	74.12%	36.45%	24.90%	18.18%
20-Day Average Volume (Shares)	324,857	413,892	2,323,115	417,980	1,091,776	409,804
EPS F1 Estimate 1-Week Change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
EPS F1 Estimate 4-Week Change	-0.20%	0.00%	0.00%	2.77%	0.35%	0.20%
EPS F1 Estimate 12-Week Change	-0.26%	1.40%	2.09%	3.87%	2.06%	0.64%
EPS Q1 Estimate Monthly Change	-1.82%	-0.12%	0.00%	1.14%	-0.28%	-0.25%

Source: Zacks Investment Research

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 maintain a 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	F
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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Returns quoted represent past performance which is no guarantee of future results. Investment returns and principal value will fluctuate so that when shares are redeemed, they may be worth more or less than their original cost. Current performance may be higher or lower than the performance shown.

Investing involves risk; principal loss is possible. There is no guarantee that companies that can issue dividends will declare, continue to pay or increase dividends.

Glossary of Terms and Definitions

52-Week High-Low: The range of the highest and lowest prices at which a stock has traded during the past year. This range is determined based on the stock's daily closing price which may differ from the intra-day high or low. Many investors use it as a technical indicator to determine a stock's current value and future price movement. The idea here is that if price breaks out from the 52-week range, in either direction, the momentum may continue in the same direction.

20-Day Average Volume (Shares): The average number of shares of a company traded in a day over the last 20 days. It is a direct indication of a security's overall liquidity. The higher the average daily trading volume, the easier it is to enter or exit the stock at a desired price with more buyers and sellers being available.

Daily Price Change: This is the percentage difference between a trading day's closing price and the prior trading day's closing price. This item is updated at 9 p.m. EST each day.

1-Week Price Change: This is the percentage change in a stock's closing price over the last 5 trading days. This change reflects the collective buying and selling sentiment over the 1-week period.

A strong weekly price increase for the stock, especially when accompanied by increased volume, is an indication of it gaining momentum.

4-Week Price Change: This is the percentage change in a stock's closing price over the last 20 trading days or past 4 weeks. This is a medium-term price change metric and an indication of the stock gaining momentum.

12-Week Price Change: This is the percentage change of a stock's closing price over the last 60 trading days or past 12 weeks. Similar to 4-week price change, this is a medium-term price change metric. It shows whether a stock has been enjoying strong investor demand, or if it has been in consolidation, or distress over this period.

52-Week Price Change: This is the percentage change in a stock's closing price over the last 260 trading days or past 52 weeks. This long-term price change metric is a good reference point for investors. Some investors seek stocks with the best percentage price change over the last 52 weeks, expecting the momentum to continue.

Market Cap: The number of outstanding common shares of a company times its latest price per share. This figure represents a company's size, which indicates various characteristics, including price stability and risk, in which investors could be interested.

Year-To-Date Price Change: Change in a stock's daily closing price in the period of time beginning the first day of the current calendar year through to the previous trading day.

of Analysts: Number of EPS estimates used in calculating the current-quarter consensus. These estimates come from the brokerage analysts tracking this stock. However, the number of such analysts tracking this stock may not match the number of estimates, as all brokerage analysts may not come up with an estimate or provide it to us.

Beta: A measure of risk commonly used to compare the volatility of a stock to the overall market. The S&P 500 Index is the base for calculating beta and carries a value of 1. A stock with beta below 1 is less risky than the market as a whole. And a stock with beta above 1 is riskier.

Dividend: The portion of earnings a company is expected to distribute to its common shareholders in the next 12 months for each share they own. Dividends are usually paid quarterly. Dividend payments reflect positively on a company and help maintain investors' trust. Investors typically find dividend-paying stocks appealing because the dividend adds to any market price appreciation to result in higher return on investment (ROI). Moreover, a steady or increasing dividend payment provides investors a cushion in a down market.

Dividend Yield: The ratio of a company's annual dividend to its share price. The annual dividend used in the ratio is calculated based on the most recent dividend paid by the company. Dividend yield is an estimate of the dividend-only return from a stock in the next 12 months. Since dividend itself doesn't change frequently, dividend yield usually changes with a stock's price movement. As a result, often an unusually high dividend yield is a result of weak stock price.

S&P 500 Index: The Standard & Poor's 500 (S&P 500) Index is an unmanaged group of securities considered to be representative of the stock market in general. It is a market-capitalization-weighted index of stocks of the 500 largest U.S. companies. Each stock's weight in the index is proportionate to its market value.

Industry: One of the 250+ groups that Zacks classifies all stocks into based on the nature of business. These groups are termed as expanded (aka "X") industries and map to their respective (economic) sectors; Zacks has 16 sectors.

Zacks Industry Rank: The Zacks Industry Rank is determined by calculating the average Zacks Rank for all stocks in the industry and then assigning an ordinal rank to it. For example, an industry with an average Zacks Rank of 1.6 is better than an industry with an average Zacks Rank of 2.3. So, the industry with the better average Zacks Rank would get a better Zacks Industry Rank. If an industry has the best average Zacks Rank, it would be considered the top industry (1 out of 250+), which would place it at the top 1% of Zacks-ranked industries. Studies have shown that roughly half of a stock's price movement can be attributed to the industry group it belongs to. In fact, the top 50% of Zacks-ranked industries outperforms the bottom 50% by a factor of more than 2 to 1.

Last EPS Surprise: The percentage deviation of a company's last reported earnings per share from the Zacks Consensus Estimate. Companies with a positive earnings surprise are more likely to surprise again in the future (or miss again if they recently missed).

Last Sales Surprise: The percentage deviation of a company's last reported sales from the Zacks Consensus Estimate.

Expected Report Date: This is an estimated date of a company's next earnings release. The information originated or gathered by Zacks Investment Research from its information providers or publicly available sources is the basis of this estimate.

Earnings ESP: The Zacks Earnings ESP compares the Most Accurate Estimate to the Zacks Consensus Estimate for the yet-to-be reported quarter. The Most Accurate Estimate is the most recent version of the Zacks Consensus EPS Estimate. The idea here is that analysts revising their estimates closer to an earnings release have the latest information, which could potentially be more accurate than what they and others contributing to the consensus had predicted earlier. Thus, a positive or negative Earnings ESP reading theoretically indicates the likely deviation of the actual earnings from the consensus estimate. However, the model's predictive power is significant for positive ESP readings only. A positive Earnings ESP is a strong predictor of an earnings beat, particularly when combined with a Zacks Rank #1 (Strong Buy), #2 (Buy) or #3 (Hold). Our research shows that stocks with this combination produce a positive surprise nearly 70% of the time.

Periods:

TTM: Trailing 12 months. Using TTM figures is an effective way of analyzing the most-recent financial data in an annualized format that helps neutralize the effects of seasonality and other quarter-to-quarter variation.

F1: Current fiscal year. This period is used to analyze the estimates for the ongoing full fiscal year.

F2: Next fiscal year. This period is used to analyze the estimates for the next full fiscal year.

F12M: Forward 12 months. Using F12M figures is an effective way of analyzing the near-term (the following four unreported quarters) estimates in an annualized manner. Instead of typically representing estimates for the full fiscal year, which may not represent the nitty-gritty of each quarter, F12M figures suggest an all-inclusive annualized estimate for the following four quarters. The annualization helps neutralize the potential effects of seasonality and other quarter-to-quarter variations.

P/E Ratio: The price-to-earnings ratio measures a company's current market price per share relative to its earnings per share (EPS). Usually, the trailing-12-month (TTM) EPS, current-fiscal-year (F1) EPS estimate, or forward-12-month (F12M) EPS estimate is used as the denominator. In essence, this ratio shows what the market is willing to pay today for each dollar of EPS. In other words, this ratio gives a sense of what the relative value of the company is at the already reported level of earnings or at a future level of earnings.

It is one of the most widely-used multiples for determining the value of a company and helps comparing its valuation with that of a competitor, the industry group or a benchmark.

PEG Ratio: The price/earnings to growth ratio is a stock's P/E ratio using current fiscal year (F1) EPS estimate divided by its expected EPS growth rate over the coming 3 to 5 years. This ratio essentially determines a stock's value by factoring in the company's expected earnings growth and is thus believed to provide a more complete picture than just the P/E ratio, particularly for faster-growing companies.

P/S Ratio: The price-to-sales ratio is calculated as a company's current price per share divided by trailing 12 months (TTM) sales or revenues per share. This ratio shows what the market is willing to pay today for each dollar of TTM sales per share. The P/S ratio is at times the only valuation metric when the company has yet to become profitable.

Cash/Price Ratio: The cash-to-price ratio or Cash Yield is calculated as cash and marketable securities per share divided by the company's current share price. Like the earnings yield, which shows the anticipated yield (or return) on a stock from earnings for each dollar invested, the cash yield does the same, with cash being the source of return instead of earnings. For example, a cash/price ratio of 0.08 suggests a return of 8% or 8 cents for every \$1 investment.

EV/EBITDA Ratio: The EV/EBITDA ratio, also known as Enterprise Multiple, is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by EBITDA (earnings before interest, taxes, depreciation and amortization). Usually, trailing-12-month (TTM) or forward-12-month (F12M) EBITDA is used as the denominator.

EV/Sales Ratio: The enterprise value-to-sales ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by annual sales. It is an expansion of the P/S valuation, which uses market value instead of enterprise value. The EV/Sales ratio is perceived as more accurate than P/S, in part, because the market capitalization does not take a company's debt into account when valuing it.

EV/CF Ratio: The enterprise value-to-cash flow ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by the trailing-12-month (TTM) operating cash flow. It's a measure of how long it would take to buy the entire business if you were able to use all the company's operating cash flow.

The EV/CF ratio is perceived as more accurate than the P/CF ratio, in part, because the market price does not take a company's debt into account when valuing it.

EV/FCF Ratio: The enterprise value-to-free cash flow metric compares a company's enterprise value to its trailing-12-month (TTM) free cash flow (FCF). This metric is very similar to the EV/CF ratio, but is considered a more exact measure owing to the fact that it uses free cash flow, which subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding growth activities and payments to shareholders.

P/EBITDA Ratio: The P/EBITDA ratio is calculated as a company's per share market value divided by EBITDA (earnings before interest, taxes, depreciation, and amortization). This metric is very similar to the EV/EBITDA ratio, but is considered a little less exact measure as it uses market price, which does not take a company's debt into account. However, since EBITDA is often considered a proxy for cash income, the metric is used as a measure of what the market is willing to pay today for each dollar of the company's cash profitability in the trailing 12 months (TTM) or forward 12 months (F12M).

P/B Ratio: The price-to-book ratio is calculated as a company's current price per share divided by its book value (total assets – liabilities – preferred stocks) per share. In short, the book value is how much a company is worth. In other words, it reflects the total value of a company's assets that its common shareholders would receive if it were to be liquidated. So, the P/B ratio indicates whether you're paying higher or lower than what would remain if the company went bankrupt immediately. Investors typically use this metric to determine how a company's stock price stacks up to its intrinsic value.

P/TB Ratio: The price-to-tangible-book value ratio is calculated as the per share market value of a company divided by the value of its tangible assets (total assets – liabilities – preferred stocks – intangible assets) per share. Tangible book value is the same thing as book value except it excludes the value of intangible assets to get a step closer to the baseline value of the company.

P/CF Ratio: The price-to-cash flow ratio measures a company's per share market price relative to its trailing-12-month (TTM) operating cash flow per share. This metric is used to determine whether a company is undervalued or overvalued relative to another stock, industry or sector. And like the P/E ratio, a lower number is typically considered better from the value perspective.

One of the reasons why P/CF ratio is often preferred over P/E ratio is the fact that operating cash flow adds back non-cash expenses such as depreciation and amortization to net income. This feature helps valuing stocks that have positive cash flow but are not profitable because of large noncash charges.

P/FCF Ratio: The price-to-free cash flow ratio is an extension of P/CF ratio, which uses trailing-12-month (TTM) free cash flow per share instead of operating cash flow per share. This metric is considered a more exact measure than P/CF ratio, as free cash flow subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding activities that generate additional revenues.

Earnings Yield: The earnings yield is calculated as current fiscal year (F1) EPS estimate divided by the company's current share price. The ratio, which is the inverse of the P/E ratio, measures the anticipated yield (or return) from earnings for each dollar invested in a stock today.

For example, earnings yield for a stock, which is trading at \$35 and expected to earn \$3 per share in the current fiscal year (F1), would be 0.0857 ($3/35 = 0.0857$) or 8.57%. In other words, for \$1 invested in the stock today, the yield from earnings is anticipated to be 8.57 cents.

Investors most commonly compare the earnings yield of a stock to that of a broad market index (such as the S&P 500) and prevailing interest rates, such as the current 10-year Treasury yield. Since bonds and stocks compete for investors' dollars, stock investors typically demand a higher yield for the extra risk they assume compared to investors of U.S. Treasury-backed securities that offer virtually risk-free returns. This additional return is referred to as the risk premium.

Debt/Equity Ratio: The debt-to-equity ratio is calculated as a company's total liabilities divided by its shareholder equity. This metric is used to gauge a company's financial leverage. In other words, it is a measure of the degree to which a company is financing its operations through debt versus its own funds. The higher the ratio, the higher the risk for shareholders.

However, this ratio is difficult to compare across industry groups where ideal amounts of debt vary. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-equity ratio should be compared with other companies in the same industry.

Cash Flow (\$/share): Cash flow per share is calculated as operating cash flow (after-tax earnings + depreciation + other non-cash charges) divided by common shares outstanding. It is used by many investors as a measure of a company's financial strength. Since cash flow per share takes into consideration a company's ability to generate cash by adding back non-cash expenses, it is regarded by some as a more accurate measure of a company's financial situation than earnings per share, which could be artificially deflated.

Current Ratio: The current ratio or liquidity ratio is a company's current assets divided by its current liabilities. It measures a company's ability to pay short-term obligations. A current ratio that is in line with the industry average or slightly higher is generally considered acceptable. A current ratio that is lower than the industry average would indicate a higher risk of distress or default. A higher number is usually better. However, a very high current ratio compared to the industry average could be an indication of inefficient use of assets by management.

Debt/Capital Ratio: Debt-to-capital ratio is a company's total debt (interest-bearing debt + both short- and long-term liabilities) divided its total capital (interest-bearing debt + shareholders' equity). It is a measure of a company's financial leverage. All else being equal, the higher the debt-to-capital ratio, the riskier the stock.

However, this ratio can vary widely from industry to industry, the ideal amount of required debt being different. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-capital ratio should be compared with the same for its industry.

Net Margin: Net margin is calculated as net income divided by sales. It shows how much of each dollar in sales generated by a company translates into profit. For example, if a company's net margin is 15%, its net income is 15 cents for every \$1 of sales it makes.

A change in margin can reflect either a change in business conditions, or a company's cost controls, or both. If a company's expenses are growing faster than sales, its net margin will decline. However, different net margin rates are considered good for different industries, so it's better to compare net margin rates of companies in the same industry group.

Return on Equity: Return on equity (ROE) is calculated as trailing-12-month net income divided by trailing-12-month average shareholder equity (including reinvested earnings). This metric is considered a measure of how effectively management is using a company's assets to generate profits. For example, if a company's ROE is 10%, it creates 10 cents profits for every \$1 shareholder equity, which is basically the company's assets minus debt. A company's ROE deemed good or bad depends on what's normal for its peers or industry group.

Sales/Assets Ratio: The sales-to-assets ratio or asset utilization ratio or asset turnover ratio is calculated as a company's annual sales divided by average assets (average of assets at the beginning of the year and at the year's end). This metric helps investors understand how effectively a company is using its assets to generate sales. For example, a sales-to-assets ratio of 2.5 indicates that the company generated \$2.50 in sales for every \$1 of assets on its books.

The higher the sales-to-assets ratio, the better the company is performing. However, similar to many other ratios, the asset turnover ratio tends to be higher for companies in certain industries/sectors than in others. So, a company's sales-to-assets ratio should be compared with the same for its industry/sector.

Historical EPS Growth (3-5 Years): This is the average annual (trailing-12-month) EPS growth rate over the last 3-5 years. This metric helps investors see how a company's EPS has grown from a long-term perspective.

Note: There are many factors that can influence short-term numbers — a recession will reduce this number, while a recovery will inflate it. The longterm perspective helps smooth out short-term events.

Projected EPS Growth (F1/F0): This is the estimated EPS growth rate for the current financial year. It is calculated as the consensus estimate for the current fiscal year (F1) divided by the reported EPS for the last completed fiscal year (F0).

Current Cash Flow Growth: It measures the latest year-over-year change in operating cash flow. Cash flow growth tells an investor how quickly a company is generating inflows of cash from operations. A positive change in the cash flow is desired and shows that more 'cash' is coming in than going out.

Historical Cash Flow Growth (3-5 Years): This is the annualized change in cash flow over the last 3-5 years. The change in a longer period helps put the current reading into proper perspective. By looking at the rate, rather than the actual dollar value, the comparison across the industry and peers becomes easier.

Projected Sales Growth (F1/F0): This metric looks at the estimated sales growth for the current year. It is calculated as sales estimate for the current fiscal year (F1) divided by the reported sales for the last completed fiscal year (F0).

Like EPS growth, a higher rate is better for sales growth. A look at a company's projected sales growth instantly tells you what the outlook is for their products and services. However, different sales growth rates are considered good for different industries, so it's better to compare sales growth rates of companies in the same industry group.

EPS F1 Estimate 1-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past week. The change in a company's consensus EPS estimate (or earnings estimate revision) has proven to be strongly correlated with the near-term price movement of its shares. It is an integral part of the Zacks Rank.

If a stock's consensus EPS estimate is \$1.10 now versus \$1.00 a week ago, that will be reflected as a 10% upward revision. If, on the other hand, it went from \$1.00 to 90 cents, that would be a 10% downward revision.

EPS F1 Estimate 4-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past four weeks.

A stock's earnings estimate revision in a 1-week period is important. But it's more meaningful to look at the longer-term revision. And, of course, the 4-week change helps put the 1-week change into proper perspective.

EPS F1 Estimate 12-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past 12 weeks.

This metric essentially shows how the consensus EPS estimate has changed over a period longer than 1 week or 4 weeks.

EPS Q1 Estimate Monthly Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal quarter over the past four weeks.

While the revision in consensus EPS estimate for the current fiscal year is strongly correlated with the near-term price movement of its shares, the estimate revision for the current fiscal quarter is an important metric as well, especially over the short term, and particularly as a stock approaches its earnings date. If a stock's Q1 EPS estimate decreases ahead of its earnings release, it's usually a negative sign, whereas an increase is a positive sign.