

Pinnacle West Capital(PNW)

\$89.49 (As of 03/02/20)

Price Target (6-12 Months): **\$101.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 05/09/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: A

Summary

Pinnacle West Capital's fourth-quarter earnings beat the Zacks Consensus Estimate, while revenues missed the same. In the past six months, the company's shares have outperformed the industry. It is well positioned to benefit from economic improvement in its service territories. The company's long-term capital expenditure plan to strengthen infrastructure and investment in battery storage projects will make its renewable projects more efficient. Cost management is also making a positive impact on margins. Apart from expanding its utility infrastructure, Pinnacle West continues to focus on enhancing its renewable capacity. However, the company is subject to comprehensive guidelines by federal, state and local regulatory agencies. Its operations are affected by fluctuations in the commodity price, weather and operational hazards.

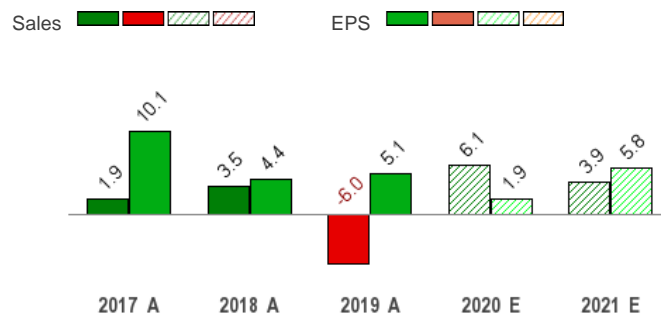
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$105.51 - \$84.26
20 Day Average Volume (sh)	1,046,044
Market Cap	\$10.7 B
YTD Price Change	5.5%
Beta	0.22
Dividend / Div Yld	\$3.13 / 3.3%
Industry	Utility - Electric Power
Zacks Industry Rank	Top 41% (105 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	21.3%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	0.1%
Expected Report Date	05/06/2020
Earnings ESP	-7.7%
P/E TTM	19.9
P/E F1	18.4
PEG F1	3.7
P/S TTM	3.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,826 E
2020	755 E	886 E	1,215 E	792 E	3,684 E
2019	741 A	870 A	1,191 A	670 A	3,471 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$5.14 E
2020	\$0.20 E	\$1.40 E	\$2.81 E	\$0.47 E	\$4.86 E
2019	\$0.16 A	\$1.28 A	\$2.77 A	\$0.57 A	\$4.77 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 03/02/2020. The reports text is as of 03/03/2020.

Overview

Phoenix, AZ-based Pinnacle West Capital Corporation was incorporated in 1985. The company provides electricity services (wholesale or retail) in the state of Arizona through its subsidiaries. The company is involved in the generation, transmission and distribution of electricity from coal, nuclear, gas, oil and solar.

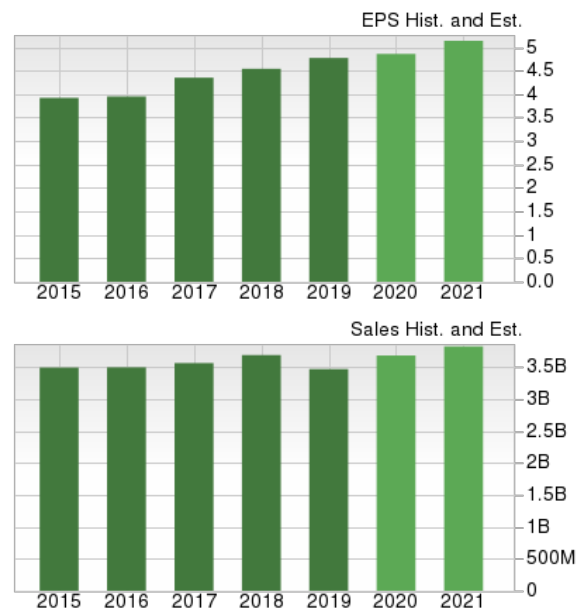
The company's only reportable segment is Regulated Electricity. The company derives 100% of its earnings from this segment. The Regulated Electricity segment consists of traditional regulated retail and wholesale electricity businesses and related activities. It includes electricity generation, transmission and distribution.

Through its wholly owned subsidiary, Arizona Public Service Company (APS), Pinnacle West transmits and distributes electricity to roughly 1.3 million residential, commercial and industrial customers. Excluding half of the Phoenix metropolitan area, the Tucson metropolitan area and Mohave County in northwestern Arizona, APS provides electric service to most of the counties in Arizona.

The company derives the majority of its revenues from APS. Pinnacle West's generation capacity owned or leased roughly 6,316 megawatts ("MW") of regulated generation and maintained a mix of both long-term and short-term power purchase agreements including purchase of renewable energy.

In 2019, the major energy sources supplied by the company were Nuclear (31.2%), followed by Gas, Oil and Other (25.5%) as well as Coal (22.7%). Meanwhile, Renewables and Purchased Power contributed 7.4% and 13.2% to the company's total power supplied, respectively.

Other subsidiaries of Pinnacle West are El Dorado Investment Company (El Dorado) and Bright Canyon Energy Corporation (BCE).



Reasons To Buy:

- ▲ In the past six months, shares of Pinnacle West have gained 0.6% against the industry's 0.5% decline. Pinnacle West carries investment grade ratings of A3 and A- by Moody's and S&P, respectively. A higher rating denotes higher credit worthiness, thereby ensuring access to cheap financing options. The solid credit rating will allow the company to secure funds from the market at favorable conditions.

Through the implementation of Lean Sigma- a cost management mechanism, the company is trying to lower O&M expenses as well as enhance customer's and shareholder's value. As a result of cost-management initiatives, the company was able to reduce O&M in 2019, despite mildest Metro Phoenix cooling season in 10 years. Pinnacle West expects to continue with its cost-savings initiatives by reducing O&M by approximately \$20 million in 2020.

Pinnacle West's investments in clean power generation, transmission & distribution lines will help it to serve customers efficiently. Improving economic conditions is also driving demand.

- ▲ Pinnacle West's subsidiary, Arizona Public Service, is the largest and longest-serving electric utility provider in Arizona. The state is witnessing a gradual economic recovery fueled by the rapidly developing Phoenix Metropolitan Area. The Metro Phoenix region continues to have job growth above the national average resulting in demand growth for utility services from commercial and residential sector. In 2019, many new companies moved into APS's service territory. The company successfully connected two new data centers to its power grid — including the Microsoft data center. Moreover, it has started preparations for adding six data center feeds in 2020.

In 2019, employment in Metro Phoenix increased 2.9% compared with 1.6% for the entire United States. Construction employment increased 9.6% and manufacturing employment rose 5.2%. Robust job growth rates continue to have a positive impact on the Metro Phoenix area's commercial and residential real estate market. APS witnessed retail customer base growth of 2.2% in the fourth quarter 2019. Based on the improving economic conditions in Arizona, the company projected its annual retail customer growth in the range of 1.5-2.5% for 2020 through 2022.

- ▲ Pinnacle West projects capital expenditure of \$1,331 million, \$1,650 million and \$1,725 million for 2020, 2021 and 2022, respectively. The company expects to invest heavily in infrastructure upgrades to serve its expanding customer base. Of the total planned capital expenditure, the company aims to invest \$1.45 billion and \$0.6 billion to upgrade and strengthen its distribution and transmission systems, respectively, in 2020-2022 time period. The ongoing investment and planned future investment will assist the company to make its systems clean, make its services affordable, reliable and developing innovative program to assist its customers.
- ▲ Apart from expanding its utility infrastructure, Pinnacle West continues to focus on enhancing its renewable capacity. As of Dec 31, 2019 Pinnacle West's renewable diverse portfolio of existing and planned renewable resources amounted to 1,923 MW, which includes solar, wind, geothermal, biomass and biogas. Of this portfolio, 1,828 MW are currently in operation and 95 MW are under construction. The company plans to invest \$1.66 billion in clean generation in the 2020-2022 time period.

The company announced its goal to deliver 100% clean carbon-free electricity to customers by 2050, which includes a near-term target of 65% clean energy by 2030 with 45% renewable energy. The company also committed to exit coal by 2031.

Reasons To Sell:

- ▼ Pinnacle West's operations are exposed to fluctuations in commodity price and transportation cost of electricity and natural gas. Potential volatility in market prices of fuel, electricity and other renewable energy commodities could create operational risks for the company. In addition, deregulation or restructuring of the electric industry may result in increased competition for the company.
- ▼ Since the company's operations are fully regulated, it has to count upon regulatory authorities for the timely recovery of investments through rate relief. Moreover, the company has nuclear generation facilities which need to undergo scrupulous safety, security and other licensing requirements. The company will be affected by unplanned outage in nuclear plants stemming from safety reasons and unexpected production stoppage.
- ▼ The company, along with its subsidiaries, is subject to numerous environmental laws and regulations, and changes in, or liabilities under, existing or new laws or regulations. Cost of complying with new regulations could increase cost of operations while failure to meet the same might impact its business.
- ▼ Unfavorable weather condition can hurt the company's profits. Fluctuation in the weather is a risk. Overall adverse weather conditions in 2019 lowered gross margin by \$37 million or 25 cents per share.

Pinnacle West's growth could be deterred by fluctuations in commodity prices, stringent environmental regulations and unplanned outages in nuclear generation facilities.

Last Earnings Report

Pinnacle West Earnings Beat Estimates in Q4, Sales Down

Pinnacle West Capital delivered adjusted earnings per share (EPS) of 57 cents in the fourth quarter of 2019, which beat the Zacks Consensus Estimate of 47 cents by 21.3%. In the year-ago quarter, the company had reported adjusted earnings of 23 cents. The bottom-line reflects improved customer growth, infrastructure investments and cost management.

In 2019, Pinnacle West Capital generated earnings of \$4.77 per share, up from \$4.54 in 2018.

Total Revenues

In the quarter under review, total revenues of \$670.4 million fell 11.4% on a year-over-year basis.

In 2019, the company delivered revenues of \$3.47 billion, down 6% from \$3.69 billion in 2018.

Operational Highlights

In fourth-quarter 2019, total operating expenses were \$658.4 million, down 4.5% from the year-ago quarter's tally.

Operating income plunged 82.1% year over year to \$11.9 million.

Interest expenses declined to \$59.6 million from \$62.2 million in the year-ago quarter.

The company set a new goal to serve APS customers with 100% clean energy by 2050.

Guidance

Management reaffirmed 2020 EPS in the range of \$4.75-\$4.95, whose mid-point of \$4.85 is in line with the current Zacks Consensus Estimate.

Quarter Ending **12/2019**

Report Date	Feb 21, 2020
Sales Surprise	NA
EPS Surprise	21.28%
Quarterly EPS	0.57
Annual EPS (TTM)	4.78

Recent News

Pinnacle West Capital to Cut 100% Emission by 2050 – Jan 22, 2020

Pinnacle West Capital Corporation announced that its subsidiary Arizona Public Service Company (“APS”) has set a target to deliver 100% clean electricity to customers by 2050. The company's nearer-term target will be to supply 65% of its total electricity from clean sources by 2030, with 45% being generated from renewable sources. Pinnacle West Capital operates through its wholly-owned subsidiary APS.

Valuation

Pinnacle West Capital shares are up 0.6% in the last six months period, and up 5.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utility sector was down 0.5% and 2.4% in the last six months period, respectively. Over the past year, the Zacks sub-industry is up up 10.6% and Zacks Utility sector is down 6.2%.

The S&P 500 index is up 1.9% in the last six months period and 7.1% in the past year.

The stock is currently trading at 19.35X of forward 12 months earnings, which compares to 13.83X for the Zacks sub-industry, 12.88X for the Zacks sector and 16.87X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.18X and as low as 14.32X, with a 5-year median of 18.15X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$101 price target reflects 20.61X of forward 12 months earnings.

The table below shows summary valuation data for PNW

Valuation Multiples - PNW					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	19.35	13.83	12.88	16.87
	5-Year High	21.18	15.58	15.36	19.34
	5-Year Low	14.32	11.14	12.58	15.18
	5-Year Median	18.15	13.27	13.8	17.44
P/S F12M	Current	2.85	2.21	2.74	3.12
	5-Year High	3.15	2.45	3.31	3.43
	5-Year Low	1.72	1.54	1.76	2.54
	5-Year Median	2.46	1.87	2.01	3.01
P/B TTM	Current	1.92	1.76	3.83	3.96
	5-Year High	2.1	2.01	4.35	4.54
	5-Year Low	1.37	1.32	2.02	2.85
	5-Year Median	1.76	1.56	2.59	3.62

As of 03/02/2020

Industry Analysis Zacks Industry Rank: Top 41% (105 out of 255)



Top Peers

Ameren Corporation (AEE)	Neutral
The AES Corporation (AES)	Neutral
Entergy Corporation (ETR)	Neutral
Alliant Energy Corporation (LNT)	Neutral
NRG Energy, Inc. (NRG)	Neutral
OGE Energy Corporation (OGE)	Neutral
Pacific Gas & Electric Co. (PCG)	Neutral
Portland General Electric Company (POR)	Neutral

Industry Comparison Industry: Utility - Electric Power				Industry Peers		
	PNW Neutral	X Industry	S&P 500	NRG Neutral	OGE Neutral	PCG Neutral
VGM Score	D	-	-	A	D	B
Market Cap	10.67 B	8.46 B	22.14 B	8.46 B	7.90 B	7.97 B
# of Analysts	3	2	13	2	2	2
Dividend Yield	3.30%	2.93%	1.98%	3.51%	3.93%	0.00%
Value Score	D	-	-	A	D	B
Cash/Price	0.00	0.05	0.05	0.05	0.00	0.19
EV/EBITDA	10.43	10.43	12.79	8.17	11.45	-1.18
PEG Ratio	4.02	3.91	1.92	0.13	4.44	1.46
Price/Book (P/B)	1.92	1.69	3.00	5.19	1.91	1.48
Price/Cash Flow (P/CF)	8.52	8.85	11.97	5.35	10.02	1.50
P/E (F1)	20.04	19.49	17.43	5.59	17.66	3.67
Price/Sales (P/S)	3.07	2.30	2.48	0.86	3.54	0.47
Earnings Yield	5.12%	5.04%	5.74%	17.88%	5.65%	27.24%
Debt/Equity	0.88	1.06	0.70	3.79	0.77	0.32
Cash Flow (\$/share)	11.14	4.21	6.94	6.39	3.94	10.06
Growth Score	D	-	-	B	F	D
Hist. EPS Growth (3-5 yrs)	6.10%	4.91%	10.85%	86.28%	9.17%	4.64%
Proj. EPS Growth (F1/F0)	1.82%	4.45%	6.48%	54.42%	3.47%	4.33%
Curr. Cash Flow Growth	-2.09%	2.98%	6.03%	19.04%	5.55%	3.97%
Hist. Cash Flow Growth (3-5 yrs)	6.02%	5.47%	8.52%	-2.48%	3.09%	5.38%
Current Ratio	0.50	0.85	1.23	1.31	0.65	1.33
Debt/Capital	46.80%	51.32%	42.57%	79.18%	43.56%	24.31%
Net Margin	15.51%	10.09%	11.57%	45.19%	19.43%	-44.64%
Return on Equity	9.80%	9.74%	16.66%	-120.17%	10.64%	21.88%
Sales/Assets	0.19	0.23	0.54	0.96	0.20	0.20
Proj. Sales Growth (F1/F0)	6.13%	2.23%	4.07%	-2.77%	0.00%	0.45%
Momentum Score	A	-	-	A	B	A
Daily Price Chg	6.06%	4.41%	3.82%	2.89%	3.62%	-2.90%
1 Week Price Chg	-13.62%	-10.97%	-12.06%	-15.65%	-15.39%	-13.50%
4 Week Price Chg	-3.39%	-5.89%	-6.43%	-8.98%	-14.04%	-12.86%
12 Week Price Chg	10.94%	3.06%	-5.15%	-11.39%	-7.17%	34.62%
52 Week Price Chg	2.05%	6.70%	4.77%	-18.08%	-6.75%	-16.62%
20 Day Average Volume	1,046,044	355,971	2,363,047	2,519,644	1,367,404	10,519,526
(F1) EPS Est 1 week change	0.14%	0.00%	0.00%	0.00%	-1.97%	0.00%
(F1) EPS Est 4 week change	0.07%	0.00%	-0.04%	9.00%	-2.61%	0.74%
(F1) EPS Est 12 week change	-1.02%	0.00%	-0.33%	7.09%	-2.83%	3.02%
(Q1) EPS Est Mthly Chg	2.63%	0.00%	-0.38%	-2.17%	NA	54.54%

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	D
Momentum Score	A
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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