

Pinnacle West Capital(PNW)

\$73.50 (As of 06/19/20)

Price Target (6-12 Months): **\$77.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 05/09/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: A

Summary

Pinnacle West Capital's ongoing investment and planned future investment will assist the company to make its systems clean, reliable and developing innovative program to assist its customers. The company has taken initiatives to lower expenses, which will allow the company to keep utility service rates low for its customers. Apart from expanding its transmission and distribution infrastructure, the company continues to focus on enhancing its renewable capacity. It carries investment grade ratings of from the credit rating agencies. However, in the past 12 months, the company's shares have underperformed the industry. It 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.

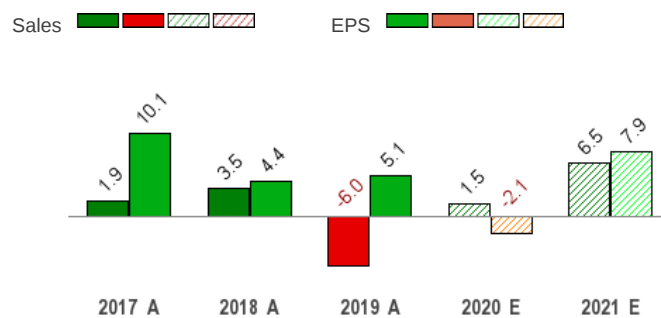
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$105.51 - \$60.05
20 Day Average Volume (sh)	1,284,577
Market Cap	\$8.3 B
YTD Price Change	-18.3%
Beta	0.37
Dividend / Div Yld	\$3.13 / 4.3%
Industry	Utility - Electric Power
Zacks Industry Rank	Top 37% (94 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	68.8%
Last Sales Surprise	-11.5%
EPS F1 Est- 4 week change	0.1%
Expected Report Date	08/13/2020
Earnings ESP	-7.6%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,751 E
2020	662 A	877 E	1,205 E	783 E	3,523 E
2019	741 A	870 A	1,191 A	670 A	3,471 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.25 E	\$1.43 E	\$2.61 E	\$0.52 E	\$5.04 E
2020	\$0.27 A	\$1.49 E	\$2.70 E	\$0.40 E	\$4.67 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.

P/E TTM	15.0
P/E F1	15.7
PEG F1	3.2
P/S TTM	2.4

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 06/19/2020. The reports text is as of 06/22/2020.

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.

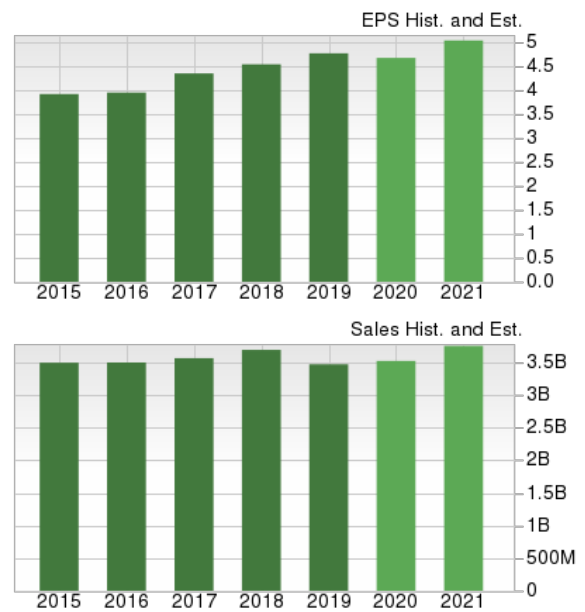
The company's only reportable segment is Regulated Electricity. The company derives 100% of its earnings from this segment. The Regulated Electricity segment consists of traditional regulated retail and wholesale electricity businesses and related activities. It includes electricity generation, transmission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

- ▲ 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. The company has ample liquidity to address \$650-million debt falling due for repayment during the second half of 2020, the company has no debt maturities in 2021-2022 time period. Pinnacle West currently has \$1.2 billion revolver capacity enough to meet its near-term obligations.

At the end of the first quarter of 2020, long-term debt was \$4,885 million compared with \$4,884 million at the end of fourth quarter of 2019. The company's times interest earned ratio came in at 3.3 at the end of the first quarter, in line with fourth-quarter 2019 levels. The strong ratio at the end of the first quarter indicates that the firm will be able to meet debt obligations in the near future without any difficulties. Moreover, its current debt to capital is 52.19% compared with the industry's average of 57.59%.

- ▲ 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. The company expects more projects to expand their business in this area in near future. For example, Red Bull announced additional 700,000-square-foot distribution center, Ball Corporation announced plans to build a second location within the Phoenix metropolitan area next to the Red Bull. White Claw/Mark Anthony Brewing Inc. announced plans to build a 916,000-square-foot facility co-located next to Red Bull in Glendale and Nacero Inc. made public plans to build a \$3.3 billion natural gas to gasoline manufacturing facility in Casa Grande.

To efficiently provide serve to increasing customer base, the company has systematic investment plans to increase generation and strengthen its transmission and distribution lines. After investing \$1,231 million in 2019, Pinnacle West has plans to invest \$1,331 million, \$1,650 million and \$1,725 million in 2020, 2021 and 2022 respectively to strengthen and expand its existing infrastructure. Based on the strength of economic conditions in Arizona and the United States, the company projected its annual retail customer growth in the range of 1.5-2.5% in 2020 through 2022.

- ▲ 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 using new technology to provide high quality service to customers, the company is also working to make cost savings, which will help to keep customer rates low. 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 the first quarter of 2020. Pinnacle West expects to continue with its cost-savings initiatives by reducing O&M by approximately \$20 million in 2020.

- ▲ Pinnacle West continues to focus on enhancing its renewable capacity. As of Mar 31, 2020 Pinnacle West's renewable diverse portfolio of existing and planned renewable resources amounted to 1,951 MW, which includes solar, wind, geothermal, biomass and biogas. Of this portfolio, 1,864 MW are currently in operation and 87 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.

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.

Reasons To Sell:

- ▼ In the past 12 months, shares of Pinnacle West have lost 24.2% wider than its industry's 8.2% decline. The company'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. First quarter 2020 revenues were impacted by milder weather.

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 Q1, Sales Down

Pinnacle West Capital delivered adjusted earnings per share of 27 cents in the first quarter of 2020, which beat the Zacks Consensus Estimate of 16 cents by 68.7%. In the year-ago quarter, the company had reported adjusted earnings of 16 cents. The bottom line reflects the impact of improved customer growth and cost management.

Total Revenues

In the quarter under review, total revenues of \$661.9 million fell 10.6% on a year-over-year basis. The figure missed the Zacks Consensus Estimate of \$748 million by 11.5%.

Operational Highlights

In first-quarter 2020, total operating expenses were \$621.5 million, down 8.6% from the year-ago quarter's tally.

Operating income declined 32.7% year over year to \$40.4 million.

Interest expenses declined to \$59.2 million from \$60.6 million in the year-ago quarter.

Guidance

Management reaffirmed 2020 EPS in the range of \$4.75-\$4.95, whose mid-point of \$4.85 is higher than the current Zacks Consensus Estimate of \$4.68.

Quarter Ending 03/2020

Report Date	May 08, 2020
Sales Surprise	-11.51%
EPS Surprise	68.75%
Quarterly EPS	0.27
Annual EPS (TTM)	4.89

Valuation

Pinnacle West Capital shares are down 18.3% in the year to date period, and down 24.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utility sector was down 13.2% and 14.9% in the year to date period, respectively. Over the past year, the Zacks sub-industry is down 8.2% and Zacks Utility sector is down 22.1%.

The S&P 500 index is down 3.8% in the year to date period and up 5.2% in the past year.

The stock is currently trading at 15.17X of forward 12 months earnings, which compares to 12.81X for the Zacks sub-industry, 12.18X for the Zacks sector and 22.24X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.18X and as low as 12.79X, with a 5-year median of 18.19X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$77 price target reflects 15.89X 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	15.17	12.81	12.18	22.24
	5-Year High	21.18	15.53	15.32	22.24
	5-Year Low	12.79	11.12	11.4	15.23
	5-Year Median	18.19	13.23	13.78	17.49
P/S F12M	Current	2.28	2.15	2.61	3.47
	5-Year High	3.15	2.45	3.29	3.47
	5-Year Low	1.72	1.54	1.75	2.53
	5-Year Median	2.46	1.89	2.05	3.02
P/B TTM	Current	1.48	1.53	3.6	4.23
	5-Year High	2.1	2.04	4.17	4.56
	5-Year Low	1.27	1.27	2.01	2.83
	5-Year Median	1.76	1.57	2.61	3.67

As of 6/19/2020

Industry Analysis Zacks Industry Rank: Top 37% (94 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Ameren Corporation (AEE)	Neutral	3
The AES Corporation (AES)	Neutral	4
Entergy Corporation (ETR)	Neutral	3
Alliant Energy Corporation (LNT)	Neutral	3
NRG Energy, Inc. (NRG)	Neutral	3
OGE Energy Corporation (OGE)	Neutral	3
Pacific GasElectric Co. (PCG)	Neutral	3
Portland General Electric Company (POR)	Neutral	4

Industry Comparison Industry: Utility - Electric Power				Industry Peers		
	PNW	X Industry	S&P 500	NRG	OGE	PCG
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	C	D	A
Market Cap	8.27 B	7.66 B	21.51 B	8.32 B	6.11 B	5.41 B
# of Analysts	3	2	14	3	2	1
Dividend Yield	4.26%	3.51%	1.92%	3.52%	5.08%	0.00%
Value Score	B	-	-	B	D	A
Cash/Price	0.01	0.06	0.06	0.10	0.02	0.34
EV/EBITDA	8.78	9.36	12.62	7.83	9.46	-0.74
PEG Ratio	3.18	3.42	2.90	0.16	3.93	1.05
Price/Book (P/B)	1.48	1.64	2.99	5.56	1.72	0.94
Price/Cash Flow (P/CF)	6.60	7.66	11.39	5.34	7.75	1.02
P/E (F1)	15.89	17.44	21.20	6.58	14.51	2.63
Price/Sales (P/S)	2.44	1.78	2.29	0.86	2.81	0.31
Earnings Yield	6.35%	5.63%	4.42%	15.20%	6.91%	37.96%
Debt/Equity	0.87	1.06	0.77	4.09	0.90	0.29
Cash Flow (\$/share)	11.14	4.15	7.01	6.39	3.94	10.06
Growth Score	C	-	-	D	D	C
Hist. EPS Growth (3-5 yrs)	6.12%	5.04%	10.87%	49.73%	10.82%	5.04%
Proj. EPS Growth (F1/F0)	-2.03%	0.51%	-10.65%	30.72%	-2.55%	-1.27%
Curr. Cash Flow Growth	-2.09%	4.96%	5.46%	19.04%	5.55%	3.97%
Hist. Cash Flow Growth (3-5 yrs)	6.02%	5.54%	8.55%	-2.48%	3.09%	5.38%
Current Ratio	0.47	0.86	1.29	1.22	0.61	1.28
Debt/Capital	46.60%	51.19%	45.14%	80.35%	47.35%	22.32%
Net Margin	16.22%	10.46%	10.53%	42.14%	-4.85%	-42.53%
Return on Equity	9.92%	9.19%	16.06%	-15,555.52%	10.86%	27.51%
Sales/Assets	0.18	0.22	0.55	0.88	0.20	0.20
Proj. Sales Growth (F1/F0)	1.49%	0.00%	-2.61%	-4.24%	0.00%	2.02%
Momentum Score	A	-	-	D	B	B
Daily Price Chg	-4.11%	-0.89%	-1.02%	1.34%	-1.42%	-5.37%
1 Week Price Chg	-4.76%	-4.10%	-7.25%	-8.28%	-8.15%	-11.98%
4 Week Price Chg	1.69%	2.07%	5.73%	-3.46%	-0.46%	-13.61%
12 Week Price Chg	-7.36%	5.04%	15.89%	20.68%	-2.65%	4.39%
52 Week Price Chg	-25.43%	-18.02%	-6.79%	-2.74%	-29.68%	-56.64%
20 Day Average Volume	1,284,577	416,783	2,574,456	2,499,622	1,762,628	12,735,481
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.14%	0.00%	0.00%	-2.88%	0.00%	0.00%
(F1) EPS Est 12 week change	-3.77%	-3.08%	-14.21%	-6.13%	-5.82%	-5.37%
(Q1) EPS Est Mthly Chg	-0.44%	-0.22%	0.00%	-3.04%	0.00%	0.00%

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	B
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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