

Pinnacle West Capital(PNW)

\$98.05 (As of 01/29/20)

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

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: C

Growth: C

Momentum: F

Summary

Pinnacle West Capital is well positioned to benefit from economic improvement in its service territories that will expand customer base and create demand. The company's long-term capital expenditure plan to strengthen infrastructure and investment in battery storage projects will make its renewable projects more efficient. It plans to invest \$4,040 million in 2019-2021 time period. Apart from expanding its utility infrastructure, Pinnacle West continues to focus on enhancing its renewable capacity. However, in the past 12 months, Pinnacle West Capital's shares have underperformed the industry. 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.

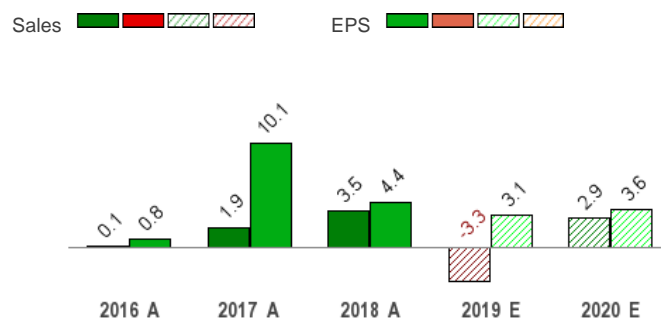
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$99.81 - \$84.26
20 Day Average Volume (sh)	840,468
Market Cap	\$11.0 B
YTD Price Change	9.0%
Beta	0.05
Dividend / Div Yld	\$3.13 / 3.2%
Industry	Utility - Electric Power
Zacks Industry Rank	Top 44% (113 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-8.6%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	-1.1%
Expected Report Date	02/21/2020
Earnings ESP	5.4%
P/E TTM	22.1
P/E F1	20.2
PEG F1	4.1
P/S TTM	3.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020					3,675 E
2019	741 A	870 A	1,191 A		3,570 E
2018	693 A	974 A	1,268 A	756 A	3,691 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.19 E	\$1.37 E	\$2.84 E	\$0.46 E	\$4.85 E
2019	\$0.16 A	\$1.28 A	\$2.77 A	\$0.47 E	\$4.68 E
2018	\$0.03 A	\$1.48 A	\$2.80 A	\$0.23 A	\$4.54 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 01/29/2020. The reports text is as of 01/30/2020.

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.

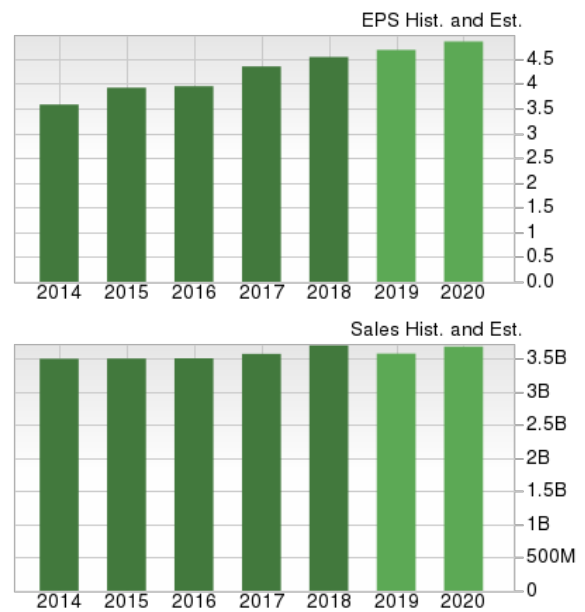
The company's only reportable segment is Regulated Electricity. The company derives 100% of its earnings from this segment. The Regulated Electricity segment consists of traditional regulated retail and wholesale electricity businesses and related activities. It includes electricity generation, transmission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

Through its wholly owned subsidiary, Arizona Public Service Company (APS), Pinnacle West transmits and distributes electricity to roughly 1.2 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 6,015 ("MW") of regulated generation and maintained a mix of both long-term and short-term power purchase agreements including purchase of renewable energy.

In 2018, the major energy sources supplied by the company were Nuclear (30.5%), followed by Gas, Oil and Other (23.5%) as well as Coal (23.2%). Meanwhile, Renewables and Purchased Power contributed 7.7% and 15.1% 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.
- ▲ 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 July, Microsoft confirmed its plans to build three world-class datacenter campuses in Goodyear in El Mirage. Construction on all three sites has begun and Microsoft will likely use 100% renewable energy to power these facilities. Nike announced its plans to build a multi-million-dollar manufacturing plant in Goodyear. Moreover, other facilities that are supporting growth in the state are Red Bull, Fairlife, Stream Data Centers, Vantage Data Centers and Compass Datacenters.

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.

Through August 2019, employment in Metro Phoenix increased 3% compared with 1.6% for the entire United States. Construction employment increased 10.8% and manufacturing employment rose 5%. Robust job growth rates continue to have a positive impact on the Metro Phoenix area's commercial and residential real estate market. In 2019, the company expects a total of 30,000 housing permits, up 10.7% compared with 2018 levels on the back of single-family permits. APS witnessed retail customer base growth of 2.1% in the third quarter. 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 2019 through 2021.

- ▲ Pinnacle West projects capital expenditure of \$1,331 million and \$1,472 million for 2020 and 2021, respectively. The expenditures will be funded through internally-generated cash flows. 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 \$1.4 billion and \$0.6 billion to upgrade and strengthen its distribution and transmission systems, respectively, in 2019-2021 time period. Grid operations and investment projected to be approximately \$1.5 billion from 2019-2021. The company is also planning to invest \$20 million through 2021 on AZ Pilot Program- EV charging, installation and maintenance for business customers, government agencies and multifamily housing communities.
- ▲ Apart from expanding its utility infrastructure, Pinnacle West continues to focus on enhancing its renewable capacity. As of Sep 30, 2019, Pinnacle West's renewable portfolio was 1,795 MW, of which 1,479 MW was solar, 289 MW was wind, 14 MW was biomass, 10 MW was geothermal and 3 MW was bio gas. The company has plans to increase renewable energy from the current levels and invest \$955 million in clean generation in the 2019-2021 time period.

The company has a history of transition and in line with this it aims to exit from Coal. Since 2005, base-line carbon emissions have been reduced 28%. Now it plans to reduce carbon intensity by 23% over the next 15 years.

Reasons To Sell:

- ▼ In the past 12 months, shares of Pinnacle West have gained 14% compared with the industry's 27.6% rise. 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. While the company's first-quarter results benefited from the weather, the same hurt third-quarter figures. Adverse weather conditions in the third quarter lowered gross margin by \$24 million or 16 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 Q3 Earnings Lag Estimates, Sales Drop Y/Y

Pinnacle West Capital Corporation's adjusted earnings of \$2.77 per share in the third quarter of 2019 missed the Zacks Consensus Estimate of \$3.03 by 8.6%. The bottom line declined 1.1% from the year-ago-quarter's earnings of \$2.80 due to unfavorable weather conditions.

Total Revenues

Total revenues came in at \$1,190.8 million, down 6% on a year-over-year basis.

Operational Highlights

In third-quarter 2019, total operating expenses of \$784.3 million fell 3.7% from \$814.4 in the year-ago quarter.

Operating income fell 6.9% year over year to \$403.3 million.

Interest expenses declined 3% to \$54 million from \$55.7 million in the year-ago quarter.

Financial Highlights

Pinnacle West had cash and cash equivalents of \$29.8 million as of Sep 30, 2019, compared with \$5.8 million as of Dec 31, 2018.

Net cash flow provided by operating activities in the first nine months of 2019 was \$834.8 million, lower than \$959.8 million in the comparable period of 2018.

Guidance

The company expects 2019 consolidated earnings will not reach the lower end of its previously reported guidance range of \$4.75 to \$4.95 per diluted share. The mid-point of the guidance, \$4.85 is higher than the current Zacks Consensus Estimate of \$4.75.

For 2020, the company predicts earnings in the range of \$4.75 to \$4.95 per diluted share.

Quarter Ending 09/2019

Report Date	Nov 07, 2019
Sales Surprise	NA
EPS Surprise	-8.58%
Quarterly EPS	2.77
Annual EPS (TTM)	4.44

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 8.4% in the last six months period, and up 14% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utility sector was up 17% and 12.5% in the last six months period, respectively. Over the past year, the Zacks sub-industry is up 27.6% and Zacks Utility sector is up 7%.

The S&P 500 index is up 11.4% in the last six months period and 22.8% in the past year.

The stock is currently trading at 20.11X of forward 12 months earnings, which compares to 15.5X for the Zacks sub-industry, 14.26X for the Zacks sector and 18.81X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.95X and as low as 14.32X, with a 5-year median of 18.11X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$104 price target reflects 21.35X 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	20.11	15.5	14.26	18.81
	5-Year High	20.95	15.5	15.33	19.34
	5-Year Low	14.32	11.19	12.61	15.18
	5-Year Median	18.11	13.09	13.7	17.45
P/S F12M	Current	2.99	2.43	3	3.49
	5-Year High	2.99	2.43	3.26	3.49
	5-Year Low	1.72	1.5	1.7	2.54
	5-Year Median	2.45	1.83	1.95	3
P/B TTM	Current	1.94	1.98	4.26	4.48
	5-Year High	2.06	1.98	4.26	4.55
	5-Year Low	1.37	1.32	2.01	2.85
	5-Year Median	1.75	1.55	2.56	3.62

As of 01/29/2020

Industry Analysis Zacks Industry Rank: Top 44% (113 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	C	B
Market Cap	11.02 B	9.17 B	23.91 B	9.35 B	9.17 B	7.96 B
# of Analysts	3	2	13	2	2	1
Dividend Yield	3.19%	2.66%	1.77%	0.32%	3.38%	0.00%
Value Score	C	-	-	A	C	A
Cash/Price	0.00	0.04	0.04	0.03	0.00	0.39
EV/EBITDA	9.57	11.68	14.07	9.88	12.52	-1.12
PEG Ratio	4.04	4.12	2.00	0.16	4.74	1.47
Price/Book (P/B)	1.94	1.78	3.27	NA	2.19	0.89
Price/Cash Flow (P/CF)	8.59	9.60	13.48	7.98	12.25	1.52
P/E (F1)	20.18	20.77	18.76	6.62	19.97	3.70
Price/Sales (P/S)	3.10	2.44	2.61	0.97	4.04	0.48
Earnings Yield	4.95%	4.72%	5.32%	15.10%	5.02%	27.04%
Debt/Equity	0.89	1.07	0.72	-4.01	0.76	0.21
Cash Flow (\$/share)	11.41	4.04	6.88	4.66	3.74	9.87
Growth Score	C	-	-	A	C	D
Hist. EPS Growth (3-5 yrs)	6.04%	4.40%	10.68%	91.38%	7.35%	4.54%
Proj. EPS Growth (F1/F0)	3.63%	5.33%	7.73%	25.64%	1.55%	1.50%
Curr. Cash Flow Growth	17.93%	7.11%	12.29%	21.62%	12.09%	7.61%
Hist. Cash Flow Growth (3-5 yrs)	6.59%	4.94%	8.78%	-1.05%	1.72%	9.17%
Current Ratio	0.71	0.80	1.23	1.24	0.79	1.79
Debt/Capital	46.99%	51.51%	43.16%	NA	43.28%	17.31%
Net Margin	14.07%	9.76%	11.59%	10.85%	19.94%	-66.15%
Return on Equity	9.19%	9.28%	17.38%	-53.61%	11.20%	18.81%
Sales/Assets	0.20	0.24	0.54	0.99	0.21	0.20
Proj. Sales Growth (F1/F0)	2.94%	3.08%	4.05%	-2.95%	NA	4.68%
Momentum Score	F	-	-	D	C	D
Daily Price Chg	1.03%	0.26%	-0.21%	0.41%	0.09%	0.67%
1 Week Price Chg	4.05%	1.12%	-1.09%	-1.50%	-0.26%	9.10%
4 Week Price Chg	9.03%	4.80%	-0.01%	-6.52%	3.06%	38.45%
12 Week Price Chg	7.55%	7.97%	4.14%	-6.11%	7.18%	117.49%
52 Week Price Chg	11.90%	18.32%	17.24%	-7.52%	13.81%	10.10%
20 Day Average Volume	840,468	301,217	1,824,613	2,289,576	1,030,913	11,445,690
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-1.09%	0.00%	0.00%	-1.06%	-0.22%	3.04%
(F1) EPS Est 12 week change	-2.93%	-0.19%	-0.11%	2.31%	0.22%	-0.97%
(Q1) EPS Est Mthly Chg	-35.59%	0.00%	0.00%	-19.30%	NA	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	C
Growth Score	C
Momentum Score	F
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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