

Sempra Energy (SRE)

\$128.22 (As of 08/19/20)

Price Target (6-12 Months): **\$136.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 08/12/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: C

Growth: F

Momentum: C

Summary

Sempra Energy ended the second quarter of 2020 on a dismal note, with both earnings and revenues missing their respective Zacks Consensus Estimate. It appears to be well-positioned for growth, given stable earnings from its utility subsidiaries. Sempra Energy continues with systematic investments in its infrastructure development projects and expects to make long-term investments of \$22.8 billion. In the past year, the company's shares also outperformed the industry. However, Sempra Energy has a current ratio of 0.80 as of Mar 31, 2020, which being less than 1, indicates that this utility may face difficulty in paying off its short-term obligations. The impacts caused by the COVID-19 pandemic have resulted in a slowdown of its capital spending, which could worsen if conditions deteriorate or fail to improve in the near term.

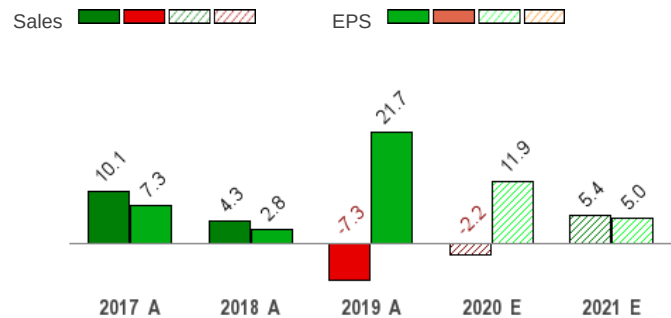
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$161.87 - \$88.00
20 Day Average Volume (sh)	1,402,873
Market Cap	\$37.1 B
YTD Price Change	-15.4%
Beta	0.72
Dividend / Div Yld	\$4.18 / 3.3%
Industry	Utility - Gas Distribution
Zacks Industry Rank	Bottom 21% (198 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-0.6%
Last Sales Surprise	-5.2%
EPS F1 Est- 4 week change	1.7%
Expected Report Date	11/06/2020
Earnings ESP	3.4%
P/E TTM	16.5
P/E F1	16.9
PEG F1	2.2
P/S TTM	3.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					11,171 E
2020	3,029 A	2,526 A	2,572 E	2,954 E	10,594 E
2019	2,898 A	2,230 A	2,758 A	2,943 A	10,829 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.85 E	\$1.28 E	\$2.07 E	\$1.69 E	\$7.97 E
2020	\$3.08 A	\$1.65 A	\$1.47 E	\$1.52 E	\$7.59 E
2019	\$1.92 A	\$1.10 A	\$1.50 A	\$1.55 A	\$6.78 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, except sales and EPS estimates, is as of 08/19/2020. The reports text and the analyst-provided sales and EPS estimates are as of 08/20/2020.

Overview

Sempra Energy is a southern California-based energy services holding company involved in the sale, distribution, storage and transportation of electricity and natural gas. The company has recently reorganized its subsidiaries under two operating groups: Sempra Utilities and Sempra Infrastructure. The Sempra Utilities group includes the company's utility operations: Southern California Gas Co. (SoCalGas), San Diego Gas & Electric (SDG&E) and Sempra South American Utilities. The Sempra Infrastructure group includes the company's energy infrastructure development activities, investments and operations: Sempra Mexico, Sempra LNG & Midstream and Sempra Renewable.

San Diego Gas & Electric (SDG&E): SoCalGas is a regulated public utility that owns and operates a natural gas distribution, transmission and storage system that supplies natural gas to a population of approximately 22 million, covering a 24,000 square mile service territory that encompasses Southern California and portions of central California. Segment earnings amounted to \$767 million in 2019, compared with \$669 million in 2018.

Southern California Gas Company (SoCalGas): SoCalGas is a regulated public utility that owns and operates a natural gas distribution, transmission and storage system that supplies natural gas to a population of approximately 22 million, covering a 24,000 square mile service territory that encompasses Southern California. Segment earnings amounted to \$641 million in 2019, compared with \$400 million in 2018.

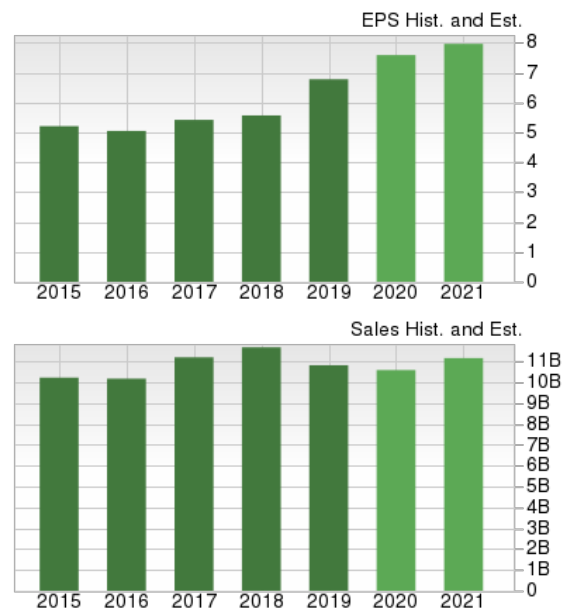
Sempra Texas Utility: Segment earnings amounted to \$528 million in 2019, compared with \$400 million in 2018..

Sempra Mexico: Segment earnings amounted to \$253 million in 2019, compared with \$237 million in 2018.

Sempra Renewables: Segment earnings amounted to \$59 million in 2019, compared with \$328 million in 2018.

Sempra LNG: The segment reported losses of \$6 million in 2019, compared with \$617 million in 2018.

Parent and Other: The segment reported losses of \$515 million in 2019 against earnings of \$620 million in 2018.



Reasons To Buy:

▲ Sempra Energy appears to be well positioned, given its stable earnings from utility subsidiaries. Moreover, the company continues with systematic investments in its infrastructure development projects. For the 2020-2024 period, the company expects to make investments of approximately \$22.8 billion including \$8.9 billion for SDG&E, \$9 billion for SoCalGas, \$0.7 billion for Sempra Texas Utility, \$1.9 billion for Sempra Mexico and \$2.3 billion for Sempra LNG. Through these investments, the company aims at vigorously modernizing its electric transmission lines and substation infrastructure.

Systematic investments in infrastructure development should bode well for Sempra Energy's growth. Also the company's progress in LNG terminal projects are appreciating

▲ As significant worldwide demand growth for LNG continues to rise, Sempra Energy is well positioned with strategically-located opportunities in North America. In LNG business, during 2019, the company made notable progress by putting Train 1 of Cameron LNG into service and starting production at Train 2. Sempra Energy is also engaged in advance commercial discussions with potential partners for its LNG development projects. In March 2020, the company finalized an engineering, procurement and construction (EPC) contract with Bechtel Corporation for its proposed Port Arthur LNG liquification project. The recent agreement will facilitate Sempra in making a final investment decision by the third quarter of 2020.

To this end, it is imperative to mention that the U.S. Energy Information Administration (EIA) expects U.S. LNG exports to continue to grow and average 7.3 Bcf/d in 2020 and 8.9 Bcf/d in 2021, as facilities gradually ramp up to full production. Sempra will certainly play an important role in the nation achieving this target, with the second and third trains of its Cameron LNG facility set to come into service this year. Moreover, in this regard, from 2020 through 2024, Sempra LNG and its joint venture with IEnova expect to make capital expenditures and investments of approximately \$2.4 billion.

▲ In an attempt to transform itself into North America's premier energy infrastructure company, in June 2020, Sempra Energy completed the sale of its Chilean asset, including its 100% interest in ChilquintaEnergía S.A., to State Grid International Development Limited for approximately \$2.23 billion in total cash proceeds. In April 2020, the sale of its Peruvian businesses was completed that generated approximately \$3.59 billion in total cash proceeds. The minority interests in Luz del Sur and Tecsur were deconsolidated upon sale of the Peruvian businesses in April 2020, and the minority interests in the ChilquintaEnergía subsidiaries were deconsolidated upon sale of the Chilean businesses in June 2020.

By divesting its non-core assets, the company aims to reinvest the proceeds into higher growth markets, namely California, Texas and Mexico, in the liquefied natural gas export markets. This, in turn, will enable Sempra Energy to focus on the delivery of cleaner and more secure forms of energy to its U.S. as well as overseas consumers. Notably, these decisions come as part of the company's Vision 2022 plan that includes a disciplined, three-phase execution of portfolio optimization and divestitures, for strengthening its focus on North American business model.

▲ Sempra Energy has consistently been paying dividends at increasing rates, courtesy of its solid cash flow from operations. Notably, its cash flow from operating activities came in at \$3,088 million at the end of 2019. Furthermore, the company hiked its dividend by 8% in February 2020. On average, Sempra has grown its dividend by more than 10% annually for the last decade, which is one of the highest dividend growth rates in the utility industry, per its management. Currently, the company sustains its annual dividend increase target at 8-9% over the next several years. Its efforts to maximize shareholder value through the payment of regular dividends will likely retain investors' interest in the stock. Further, in the past year, shares of Sempra Energy have outperformed the industry. Its shares have dropped 8.9% compared with the industry's decline of 24.4%.

Reasons To Sell:

- ▼ The current U.S. Administration indicated its intention to revise or replace international trade agreements, such as North American Free Trade Agreement (NAFTA). In November 2018, President Trump signed the United States, Mexico-Canada Agreement (USMCA), which, if approved by the legislatures of the U.S., Mexico and Canada, would replace NAFTA. U.S. and Mexico approved the USMCA in January 2020 and June 2019, respectively, but Canada is yet to give its approval. A shift in U.S. trade policies could materially affect Sempra's LNG development opportunities, as well as trade opportunities between Mexico and the United States.
- ▼ Sempra Energy has a long-term debt of \$20,535 million as of June 30, 2020, higher than \$20,198 million as of Mar 31, 2020. The company's cash equivalents for the period remained much lower compared to its current debt levels. As of June 30, 2020, its cash equivalents were \$4,927 million. While the long-term debt level lies much above the company's cash reserve, its current debt worth \$5,428 as of June 30, 2020 also remains higher than the cash balance. Therefore, as both the long-term and current debt values of the company lie much above its cash reserve, this reflects a weak solvency position on the company's part and makes us skeptical about its ability to duly meet its obligations. Moreover, the company has a current ratio of 0.80 as of Mar 31, 2020, which being less than 1, indicates that this utility may face difficulty in paying off its short-term obligations.
- ▼ A comparative analysis of the company's forward 12-month Price/Sales ratio indicates a relatively gloomy picture that might be a cause for investors' concern. Consequently, the stock currently has a trailing 12-month Price/Sales ratio of 3.35. The level compares unfavorably when compared to its historical levels. Also, the company's Price/Sales ratio has been above the industry's Price/Sales ratio of 2.01 in the past year.
- ▼ The impacts caused by the COVID-19 pandemic has resulted in a slowdown of its capital spending, which could worsen if conditions deteriorate or fail to improve in the near term. In the second quarter itself, its final investment decision on Phase 1 of the proposed ECA LNG JV natural gas liquefaction project got delayed due to the closure of non-essential activities in Mexico in response to the COVID-19 pandemic. Notably, if this or other projects under development are further delayed due to the COVID-19 pandemic or other related factors, the performance and prospects of its LNG export business could be negatively impacted. Overall, this could have a material adverse effect on Sempra Energy's results of operations and since the pandemic is still going on, chances of a stark rebound from this crisis seems very bleak.

Possible shift in U.S. trade policies and unfavorable financial ratios could hurt the company's performance in the future.

Last Earnings Report

Sempra Energy Q2 Earnings Miss, Revenues Improve Y/Y

Sempra Energy's second-quarter 2020 adjusted earnings per share (EPS) came in at \$1.65, which missed the Zacks Consensus Estimate of \$1.66 by 0.6%. The bottom line, however, soared 50% from \$1.10 reported in the prior-year quarter.

Barring one-time items, the company generated GAAP earnings of \$7.61 per share compared with GAAP earnings of \$1.26 reported in second-quarter 2019.

Quarter Ending **06/2020**

Report Date	Aug 05, 2020
Sales Surprise	-5.16%
EPS Surprise	-0.60%
Quarterly EPS	1.65
Annual EPS (TTM)	7.78

Total Revenues

In the quarter under review, total revenues of \$2,526 million increased 13.3% year over year on higher contributions from its Utilities (up 17.8%) business. The top line, however, missed the consensus mark of \$2,663 million by 5.1%.

Segment Update

San Diego Gas & Electric (SDG&E): Quarterly earnings amounted to \$193 million compared with the year-ago quarter's \$143 million.

Southern California Gas Company (SoCalGas): In this segment, earnings totaled \$146 million in the second quarter of 2020 compared with \$30 million registered in the prior-year quarter.

Sempra Texas Utility: Earnings in this segment came in at \$144 million in the reported quarter compared with \$113 million in the year-ago quarter.

Sempra Mexico: The segment recorded net earnings of \$61 million compared with \$73 million in the year-ago quarter.

Sempra LNG: The segment reported earnings of \$61 million compared with the year-ago quarter's \$6 million.

Parent and Other: Quarterly loss at this division rose to \$141 million from the year-ago quarter's loss of \$127 million.

Financial Update

As of Jun 30, 2020, Sempra Energy's cash and cash equivalents totaled \$4,894 million compared with \$108 million as of Dec 31, 2019.

Long-term debt and finance leases amounted to \$20,535 million as of Jun 30, 2020, compared with \$20,785 million at 2019-end.

Cash flow from operating activities was \$1,027 million at the end of second-quarter 2020, down from \$1,704 million at the end of second-quarter 2019.

In the reported quarter, the company's total capital expenditures, investments and acquisitions summed \$1,242 million compared with \$2,165 million in the second quarter of 2019.

2020 Guidance

Sempra Energy updated its adjusted EPS guidance for 2020. The company expects to generate earnings of \$7.20-\$7.80 per share. The Zacks Consensus Estimate for full-year earnings stands at \$7.54 per share, above the midpoint of the company-projected view.

Recent News

On **Jun 30, 2020**, Sempra Energy announced that it has completed its business exit from South America, following the recently announced sale of its Chilean businesses, which generated approximately \$2.23 billion in total cash proceeds, subject to post-closing adjustments. The completion of the Chilean transactions concludes Sempra Energy's sales of its South American businesses in both Chile and Peru, resulting in approximately \$5.82 billion in combined total cash proceeds, subject to customary post-closing adjustments. The company's investments are now focused in top-tier markets in North America.

On **June 22, 2020**, Southern California Gas Co. (SoCalGas), Pacific Gas and Electric Company and Opus 12 announced that they have demonstrated further advancement of a new electrochemical technology that converts the carbon dioxide content in raw biogas to pipeline-quality renewable natural gas, a critical improvement in the science of upgrading waste emissions to renewable gas. The single-step process is designed to use renewable electricity, and thus also provides a way for long-term storage of excess wind and solar power. The twelve-month research and development effort was funded by SoCalGas and PG&E and builds on the success of an initial feasibility study in 2018.

Valuation

Sempra Energy's shares are down 15.4% in the year-to-date period and 8.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utilities sector are down 27.5% and 13.8% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 24.4% whereas the sector is down 9.9%.

The S&P 500 index is up 4.7% in the year-to-date period and 15.6% in the past year.

The stock is currently trading at 16.4X of forward 12-month earnings, which compares to 14.3X for the Zacks sub-industry, 12.7X for the Zacks sector and 22.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 24.9X and as low as 12.2X, with a 5-year median of 20X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$136 price target reflects 17.3X forward 12-month earnings.

The table below shows summary valuation data for SRE

Valuation Multiples - SRE					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	16.35	14.25	12.68	22.78
	5-Year High	24.92	23.03	15.28	22.78
	5-Year Low	12.18	12.59	11.3	15.25
	5-Year Median	20.01	20.39	13.72	17.58
P/S F12M	Current	3.38	1.77	2.68	3.7
	5-Year High	4.02	2.3	3.29	3.7
	5-Year Low	1.72	1.02	1.75	2.53
	5-Year Median	2.54	4.69	2.07	3.05
EV/EBITDA TTM	Current	12.3	11.91	18.54	12.76
	5-Year High	16.63	14.73	21.06	12.85
	5-Year Low	10.33	10.05	10.59	8.25
	5-Year Median	12.87	12.63	13.92	10.91

As of 08/19/2020

Industry Analysis Zacks Industry Rank: Bottom 21% (198 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Atmos Energy Corporation (ATO)	Neutral	3
Consolidated Edison Inc (ED)	Neutral	4
ONE Gas, Inc. (OGS)	Neutral	4
Public Service Enterprise Group Incorporated (PEG)	Neutral	3
Southwest Gas Corporation (SWX)	Neutral	3
UGI Corporation (UGI)	Neutral	2
NewJersey Resources Corporation (NJR)	Underperform	3
ONEOK, Inc. (OKE)	Underperform	4

Industry Comparison Industry: Utility - Gas Distribution				Industry Peers		
	SRE	X Industry	S&P 500	ATO	OGS	OKE
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Underperform
Zacks Rank (Short Term)	3	-	-	3	4	4
VGM Score	D	-	-	D	D	B
Market Cap	37.09 B	3.86 B	23.61 B	12.66 B	3.93 B	12.38 B
# of Analysts	6	3	14	5	4	5
Dividend Yield	3.26%	3.48%	1.65%	2.24%	2.91%	13.42%
Value Score	C	-	-	D	C	A
Cash/Price	0.13	0.06	0.07	0.02	0.00	0.07
EV/EBITDA	12.75	10.78	13.36	14.71	11.65	9.85
PEG Ratio	2.20	3.01	2.99	3.01	3.82	3.64
Price/Book (P/B)	1.69	1.73	3.16	1.94	1.79	1.98
Price/Cash Flow (P/CF)	10.26	8.88	12.71	13.30	10.68	6.56
P/E (F1)	16.89	16.29	21.82	21.83	21.03	21.83
Price/Sales (P/S)	3.30	1.64	2.47	4.54	2.62	1.42
Earnings Yield	5.92%	6.03%	4.37%	4.58%	4.76%	4.59%
Debt/Equity	0.92	0.97	0.76	0.70	0.72	2.30
Cash Flow (\$/share)	12.50	4.07	6.94	7.72	6.96	4.25
Growth Score	F	-	-	C	D	C
Hist. EPS Growth (3-5 yrs)	7.94%	7.73%	10.44%	9.06%	10.58%	19.23%
Proj. EPS Growth (F1/F0)	11.95%	1.18%	-5.97%	8.09%	0.71%	-58.44%
Curr. Cash Flow Growth	12.92%	10.67%	5.22%	12.19%	10.48%	11.06%
Hist. Cash Flow Growth (3-5 yrs)	8.55%	8.55%	8.52%	11.14%	9.29%	22.18%
Current Ratio	0.80	0.79	1.33	0.86	0.71	1.71
Debt/Capital	44.72%	49.25%	44.50%	41.22%	41.92%	69.72%
Net Margin	38.49%	7.55%	10.13%	21.31%	12.35%	7.13%
Return on Equity	11.47%	9.37%	14.67%	9.31%	8.62%	18.28%
Sales/Assets	0.17	0.27	0.51	0.19	0.27	0.40
Proj. Sales Growth (F1/F0)	-2.17%	-1.09%	-1.54%	3.23%	-5.61%	-10.74%
Momentum Score	C	-	-	D	C	D
Daily Price Chg	-0.88%	-0.35%	-0.38%	-0.35%	-0.52%	-0.78%
1 Week Price Chg	1.53%	0.00%	1.09%	-1.14%	-1.96%	0.07%
4 Week Price Chg	0.27%	-1.34%	2.23%	-1.34%	-4.32%	-5.56%
12 Week Price Chg	2.66%	-5.34%	6.91%	3.49%	-9.63%	-25.90%
52 Week Price Chg	-8.95%	-24.01%	2.28%	-7.60%	-18.31%	-60.86%
20 Day Average Volume	1,402,873	352,151	1,899,976	806,929	213,435	5,259,435
(F1) EPS Est 1 week change	0.47%	0.00%	0.00%	0.00%	0.00%	-0.81%
(F1) EPS Est 4 week change	1.67%	0.06%	1.70%	0.13%	-0.14%	-6.37%
(F1) EPS Est 12 week change	4.79%	-0.28%	3.08%	0.20%	-0.84%	-13.96%
(Q1) EPS Est Mthly Chg	-7.40%	-2.03%	0.83%	-2.03%	-0.48%	-6.95%

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	F
Momentum Score	C
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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