

Sempra Energy (SRE)

\$160.06 (As of 01/23/20)

Price Target (6-12 Months): **\$170.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/11/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: A

Summary

Sempra Energy appears to be well-positioned for growth, given its stable earnings from utility subsidiaries. The company continues with systematic investments in its infrastructure development projects and expects to make capital expenditure and investments of \$18.2 billion. Through these investments, it aims at vigorously modernizing its electric transmission lines and substation infrastructure. In the past year, the stock has outperformed its industry. However, its operations are subject to risks associated with the breakdown or failure of equipment. Also, it bears a notable long-term debt and finance leases of \$3.78 billion at the third quarter end. Such massive debt levels might hurt the company going ahead. Lowering credit ratings assigned to the company by major credit rating agencies remain a cause of concern.

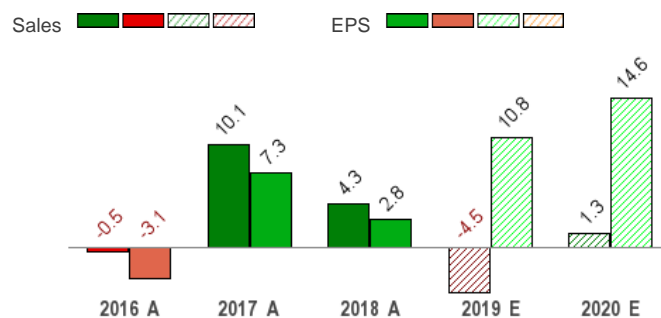
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$160.18 - \$112.02
20 Day Average Volume (sh)	1,067,361
Market Cap	\$45.1 B
YTD Price Change	5.7%
Beta	0.41
Dividend / Div Yld	\$3.87 / 2.4%
Industry	Utility - Gas Distribution
Zacks Industry Rank	Top 41% (104 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.7%
Last Sales Surprise	-5.6%
EPS F1 Est- 4 week change	0.4%
Expected Report Date	02/25/2020
Earnings ESP	0.0%
P/E TTM	26.3
P/E F1	22.6
PEG F1	3.0
P/S TTM	4.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020					11,305 E
2019	2,898 A	2,230 A	2,758 A	3,084 E	11,163 E
2018	2,962 A	2,564 A	2,940 A	3,221 A	11,687 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$1.97 E	\$1.24 E	\$2.24 E	\$1.66 E	\$7.07 E
2019	\$1.92 A	\$1.10 A	\$1.50 A	\$1.31 E	\$6.17 E
2018	\$1.43 A	\$1.35 A	\$1.23 A	\$1.56 A	\$5.57 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 01/23/2020. The reports text is as of 01/24/2020.

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): Segment earnings amounted to \$669 million in 2018, compared to \$407 million in 2017.

Southern California Gas Company (SoCalGas): Segment earnings amounted to \$400 million in 2018, compared to \$396 million in 2017.

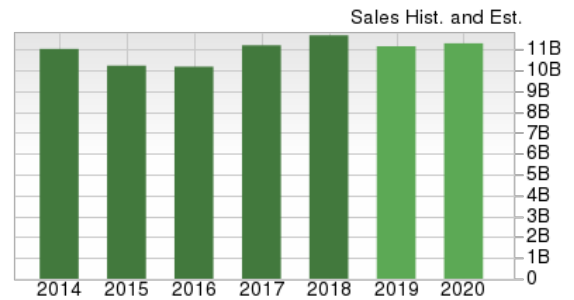
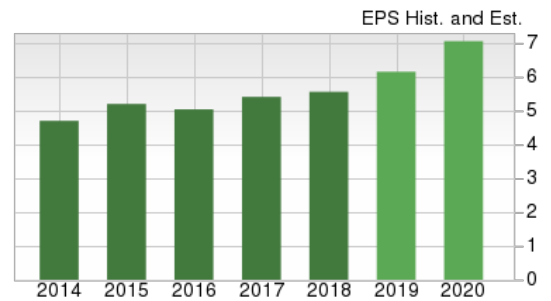
Sempra Texas Utility: Segment earnings amounted to \$371 million in 2018.

Sempra Mexico: Segment earnings amounted to \$237 million in 2018, compared to \$169 million in 2017.

Sempra Renewables: Segment earnings amounted to \$328 million in 2018, compared to \$252 million in 2017.

Sempra LNG: The segment reported losses of \$617 million in 2018, against the earnings of \$150 million in 2017.

Parent and Other: The segment reported losses of \$663 million in 2018, against the earnings of \$1,304 million in 2017.



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 2019-2023 period, the company expects to make investments of approximately \$18.2 billion including \$13.3 billion for California Utilities and \$4.9 billion for other subsidiaries to fund the capital projects in Mexico and South America along with the development of LNG projects. Through these investments, the company aims at vigorously modernizing its electric transmission lines and substation infrastructure.

The recent acquisitions should bode well for Sempra Energy's growth. Also the company's progress in LNG terminal projects are appreciating

▲ In May 2019, Sempra Energy's Oncor acquired InfraREIT and its subsidiaries for an aggregate purchase price of approximately \$1.33 billion. Following the buyout, the company is expanding its footprint in Texas by adding various electricity transmission and distribution assets, and projects in the north, central, west and panhandle regions of Texas. In May, the company also acquired an indirect 50% interest in Sharyland Holdings for \$102 million. Notably, Sharyland owns a regulated electric transmission and distribution utility serving customers near the Texas-Mexico border. Such notable buyouts will enhance the service territory of Sempra Energy, expanding its opportunities to earn more profit. These together may have led the company to outperform its industry in the past twelve months. Shares of Sempra Energy have surged 45.6% compared with the industry's 21.7% growth.

▲ In an attempt to transform itself into a leading energy company, toward the end of September, the company signed an agreement to divest stake in its Peruvian businesses to China Yangtze Power International. Sempra Energy is expected to earn cash worth \$3.59 billion from this deal. Furthermore, in October, Sempra Energy signed an agreement to divest equity stake in its Chilean businesses to State Grid International Development Limited (SGID). Sempra Energy will receive \$2.23 billion in cash from the deal. With this divestiture, Sempra Energy aims to use the sale proceeds for capital investment in the United States and Mexico, in order to support additional growth opportunities. This divestment is also expected to strengthen the company's balance sheet by paying down parent debt.

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. Per this plan, Sempra Energy expects to witness a solid 13% annualized growth in its earnings per share (EPS) for the period of 2019-2022.

▲ As the significant worldwide demand growth for LNG continues to rise, Sempra Energy is well positioned with strategically-located opportunities in North America. In May 2019, the company completed construction of the first of large-scale, three-train natural gas liquefaction project – Cameron. Also, the first commissioning cargo carrying LNG was shipped. In July, Cameron LNG JV received authorization from the FERC to place Train 1 in service. Production from Train 2 and 3 is expected in the first and second quarters of 2020. Moreover, Sempra Energy continues to advance its LNG development projects including signing the heads of agreement with Aramco Services Company at Port Arthur LNG. Such notable accomplishments should boost its global LNG business in the long-term.

▲ 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 \$1,829 million at the end of third-quarter 2019. Furthermore, the company posted dividend hike of 8.1% in February 2019. Currently, it pays an annual dividend of \$3.87 per share, up from \$3.58 paid earlier. During the nine months of 2019, the company paid dividends of \$734 million, up 13.8% year over year. 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.

Reasons To Sell:

- ▼ At the end of the third quarter, Moody's issuer rating was Baa1, with a negative outlook for Sempra Energy, Baa1 with a positive outlook for SDG&E and A1 with a negative outlook for SoCalGas. Also, S&P issuer credit rating was BBB+, with a negative outlook for Sempra Energy, BBB+ with a stable outlook for SDG&E, and A with a negative outlook for SoCalGas. The rating actions primarily reflected the persistent execution risk as Sempra Energy carries out plans to sell its South American utilities. Also, the delays at the Cameron LNG JV facilities, SDG&E's exposure to wildfire risk in California and the potential impact on Sempra Energy's financial credit metrics, got reflected in the poor credit ratings. These recent actions or any additional negative outlook on the company's credit ratings may adversely impact Sempra Energy's credibility to borrow funds, going ahead.
- ▼ The Aliso Canyon gas leak is a massive leak from a natural gas well connected to the Aliso Canyon underground storage facility near Porter Ranch, Los Angeles, CA since Oct 23, 2015. Aliso Canyon is the second largest gas storage facility of its kind in the U.S. and belongs to the Southern California Gas Company, a unit of Sempra Energy. The facility represents 63% of the SoCalGas-owned natural gas storage capacity. On Jan 6, 2016, Governor Jerry Brown issued a state of emergency. SS25, the leaking well, was permanently sealed on Feb 18, 2016. As of Sep 30, 2019, SoCalGas incurred estimated costs of \$54 million related to the leak. These costs may rise considerably as more information becomes available and could have a material impact on cash flows, financial condition and results of operations at both Sempra Energy and SoCalGas.
- ▼ Sempra Energy's operations are subject to risks associated with breakdown or failure of equipment or processes due to fuel supply or transportation disruptions, natural calamities and accidents. The company will face operational difficulties in case of any such event.
- ▼ The company already bears a notable long-term debt and finance leases of \$3.78 billion as of Sep 30, 2019. Such massive debt levels can turn out to be a major headwind for the company going ahead. This is because investors try to avoid high debt burden stocks as they are more prone to bankruptcy in times of crisis. Moreover, with the current U.S. economy being in favor of the expanding interest rate, the credit market may not turn out to be much favorable for Sempra Energy.
- ▼ 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 3.85. 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 2.47 in the past year.

Poor credit rating and several operational risks could hurt the company's performance in the future.

Last Earnings Report

Sempra Energy Beats on Q3 Earnings, Ups '19 EPS View

Sempra Energy's third-quarter 2019 adjusted earnings per share (EPS) came in at \$1.50, which surpassed the Zacks Consensus Estimate of \$1.49 by 0.7%. The bottom line also improved 22% from \$1.23 registered in the prior-year quarter.

Barring one-time items, the company generated GAAP earnings of \$2.84 per share compared with 99 cents in third-quarter 2018. This uptick can be attributed to year-over-year revenue and operating income growth.

Quarter Ending **09/2019**

Report Date	Nov 01, 2019
Sales Surprise	-5.62%
EPS Surprise	0.67%
Quarterly EPS	1.50
Annual EPS (TTM)	6.08

Total Revenues

In the quarter under review, total revenues of \$2,758 million increased 7.5% year over year on higher contributions from its Utilities (up 14.1%) business. The top line, however, missed the consensus mark of \$2,922 million by 5.6%.

Segment Update

San Diego Gas & Electric (SDG&E): Quarterly earnings amounted to \$263 million compared with the year-ago quarter's \$205 million.

Southern California Gas Company (SoCalGas): At this segment, quarterly earnings totaled \$143 million in the third quarter of 2019 compared with \$14 million registered in the prior-year quarter.

Sempra Texas Utility: Earnings at this segment came in at \$212 million in the reported quarter compared with \$154 million in the year-ago quarter.

Sempra Mexico: The segment recorded net earnings of \$84 million compared with \$44 million in the year-ago quarter.

Sempra Renewables: The segment did not record any earnings in the third quarter against earnings of \$34 million in the third quarter of 2018.

Sempra LNG: The segment reported earnings of \$2 million compared with the year-ago quarter's \$16 million.

Parent and Other: Quarterly loss at this division narrowed to \$139 million from the year-ago quarter's loss of \$211 million.

Financial Update

As of Sep 30, 2019, Sempra Energy's cash and cash equivalents totaled \$106 million compared with \$102 million as of Dec 31, 2018.

Long-term debt and finance leases amounted to \$20,995 million as of Sep 30, 2019 compared with \$20,903 million at 2018 end.

Cash flow from operating activities was \$1,829 million at the end of third-quarter 2019, down from \$2,439 million at the end of third-quarter 2018. In the reported quarter, the company's total capital expenditures, investments and acquisitions were \$997 million compared with \$918 million in the third quarter of 2018.

Highlights of the Quarter

In September, Sempra LNG entered into a memorandum of understanding (MOU) with China Three Gorges Corporation regarding potential cooperation for the supply of LNG to support demand in China, including growth of natural gas power generation.

In August, the Cameron LNG liquefaction-export project in Hackberry, LA began commercial operations at Train 1 of the facility. The project, including Trains 2 and 3, is over 96% complete. Commissioning of Train 2 is underway and the previously disclosed project timeline remains unchanged.

2019 Guidance

Sempra Energy raised its earnings guidance for 2019. The company currently expects to generate earnings of \$6.00-\$6.50 per share compared with the earlier guidance range of \$5.70-\$6.30. The Zacks Consensus Estimate for full-year earnings stands at \$6.08, lower than the midpoint of the company projected view.

Valuation

Sempra Energy's shares are up 7.7% in the past six months period and up 34.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Utilities sector are up 2.1% and 3.6% in the past six months period, respectively. Over the past year, the Zacks sub-industry is up 20.1% , whereas the sector is up 4.9%.

The S&P 500 index is up 10.8% in the past six months period and is up 28% in the past year.

The stock is currently trading at 22.57X of forward 12-month earnings, which compares to 20.66X for the Zacks sub-industry, 14.18X for the Zacks sector and 19.15X for the S&P 500 index.

Over the past five years, the stock has traded as high as 24.92X and as low as 16.40X, with a 5-year median of 20.42X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$170 price target reflects 23.89X 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	22.57	20.66	14.18	19.15
	5-Year High	24.92	23.03	15.33	19.34
	5-Year Low	16.4	16.66	12.61	15.17
	5-Year Median	20.4	20.42	13.7	17.44
P/S F12M	Current	4.02	2.34	3.03	3.56
	5-Year High	4.02	2.34	3.26	3.56
	5-Year Low	1.72	0.98	1.7	2.54
	5-Year Median	2.47	1.6	1.95	3
P/B TTM	Current	2.47	1.7	4.23	4.55
	5-Year High	2.47	2.29	4.23	4.55
	5-Year Low	1.55	1.01	2.01	2.85
	5-Year Median	1.95	1.69	2.56	3.62

As of 01/24/2020

Industry Analysis Zacks Industry Rank: Top 41% (104 out of 255)



Top Peers

Atmos Energy Corporation (ATO)	Neutral
Consolidated Edison Inc (ED)	Neutral
NewJersey Resources Corporation (NJR)	Neutral
Northwest Natural Gas Company (NWN)	Neutral
ONE Gas, Inc. (OGS)	Neutral
ONEOK, Inc. (OKE)	Neutral
Southwest Gas Corporation (SWX)	Underperform
UGI Corporation (UGI)	Underperform

Industry Comparison Industry: Utility - Gas Distribution				Industry Peers		
	SRE Neutral	X Industry	S&P 500	ATO Neutral	OGS Neutral	OKE Neutral
VGM Score	D	-	-	D	D	D
Market Cap	45.12 B	4.69 B	24.46 B	14.29 B	5.05 B	31.51 B
# of Analysts	4	2	13	4	3	9
Dividend Yield	2.42%	2.75%	1.75%	1.97%	2.09%	4.80%
Value Score	D	-	-	D	C	C
Cash/Price	0.00	0.01	0.04	0.00	0.00	0.02
EV/EBITDA	19.39	13.64	14.11	15.41	14.47	17.94
PEG Ratio	2.95	3.17	2.04	3.49	4.42	1.89
Price/Book (P/B)	2.47	2.16	3.40	2.40	2.40	5.07
Price/Cash Flow (P/CF)	13.78	12.26	13.66	15.14	15.14	19.86
P/E (F1)	22.64	20.27	19.10	24.96	26.50	20.17
Price/Sales (P/S)	4.06	1.98	2.67	4.92	3.03	2.96
Earnings Yield	4.42%	4.82%	5.23%	4.00%	3.77%	4.95%
Debt/Equity	1.15	0.99	0.72	0.61	0.61	2.01
Cash Flow (\$/share)	11.61	3.40	6.94	7.72	6.33	3.84
Growth Score	D	-	-	C	D	C
Hist. EPS Growth (3-5 yrs)	3.77%	5.57%	10.60%	9.06%	12.67%	16.83%
Proj. EPS Growth (F1/F0)	14.71%	9.36%	7.59%	7.64%	3.24%	23.64%
Curr. Cash Flow Growth	11.20%	7.46%	13.90%	12.19%	7.90%	68.93%
Hist. Cash Flow Growth (3-5 yrs)	7.97%	6.65%	9.00%	11.14%	6.38%	15.84%
Current Ratio	0.39	0.77	1.22	0.38	0.57	1.26
Debt/Capital	50.53%	49.94%	42.99%	38.03%	37.96%	66.79%
Net Margin	23.55%	8.72%	11.35%	17.62%	10.83%	11.76%
Return on Equity	10.12%	8.85%	17.10%	9.19%	8.63%	19.56%
Sales/Assets	0.18	0.35	0.55	0.23	0.30	0.54
Proj. Sales Growth (F1/F0)	1.27%	4.80%	4.03%	20.02%	4.63%	8.14%
Momentum Score	A	-	-	F	F	D
Daily Price Chg	1.59%	0.68%	0.26%	0.68%	0.75%	0.91%
1 Week Price Chg	4.97%	3.22%	2.29%	3.22%	3.27%	2.17%
4 Week Price Chg	5.57%	2.50%	2.24%	5.77%	3.48%	0.21%
12 Week Price Chg	10.76%	3.91%	7.79%	3.91%	3.15%	9.25%
52 Week Price Chg	41.21%	6.66%	21.61%	20.91%	14.96%	21.77%
20 Day Average Volume	1,067,361	338,637	1,536,379	631,276	214,311	1,536,379
(F1) EPS Est 1 week change	0.21%	0.00%	0.00%	0.32%	-1.09%	-0.03%
(F1) EPS Est 4 week change	0.42%	0.00%	0.00%	0.41%	-1.09%	0.50%
(F1) EPS Est 12 week change	3.82%	-0.13%	-0.23%	1.08%	-1.34%	-0.01%
(Q1) EPS Est Mthly Chg	35.52%	-0.23%	0.00%	-1.05%	-0.56%	-2.42%

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	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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