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A Financial Analysis and Valuation of Energy Transfer LP

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Abstract: This paper presents a thorough financial analysis of Energy Transfer LP aimed at enhancing investors' comprehension of the company's financial standing and stock potential. Additionally, it provides insights into the company's current market position and detailed corporate information, serving as a guide for investors unfamiliar with the natural gas market in making informed investment decisions. The article also examines potential risks impacting the company's stock and proposes actionable investment recommendations. While Energy Transfer LP exhibits promising stock potential and a notable rate of return, analysis reveals inherent risks within its operational structure. Mitigating these risks through strategic enhancements could amplify its attractiveness to financial investors. Furthermore, given the significant influence of external factors, particularly public sentiment towards energy companies, investors are advised to conduct thorough investigations into the stability of the natural gas market's development trajectory in the coming years before making investment decisions. This paper underscores the importance of strategic planning to mitigate operational risks and emphasizes the necessity of comprehensive market analysis for informed investment decisions in the energy sector.

Keywords: Energy Transfer LP, Financial Analysis, Valuation, Risk Assessment

1. Introduction

North America plays an important role in the global natural gas market. According to statistics, North America's natural gas supply accounts for 26.2% of the world's total natural gas supply, ranking first in the world, and its global share is increasing year by year [1]. North America is characterized by its extensive geographical scope and rich resources, which includes the United States, Canada and Mexico. Among these three countries, the proportion of natural gas supply in the United States is far greater than that in the other two countries, reaching 79.3% of the natural gas supply in North America, compared with 12.8% in Canada and 7.9% in Mexico. However, the close connection between these three countries makes the whole North American natural gas market highly integrated, and the establishment of pipelines and infrastructure of energy companies facilitates the movement of natural gas across borders [2].

Among the different energy companies, Energy Transfer LP has attracted wide attention because of its considerable scale and rich business. The midstream energy sector in which this company is located is very important for the whole energy value chain because it is the link between energy producers and consumers, and it ensures the efficiency and reliability of energy resources transportation in the whole country [3]. This company operates in all states of the United States. In addition to building a large number of natural gas transportation pipelines and natural gas storage facilities in Texas and Oklahoma, it sells natural gas to end users such as power companies and power plants. Besides, Energy Transfer LP has natural gas collection pipelines and processing plants in other states in the United States, and its products also include natural gas liquid (NGL), coal, crude oil and petroleum. The various products have prompted Energy Transfer to show strong financial performance in recent years, and reached the 53rd place in the top 500 financial companies in the United States. The company's revenue is primarily generated from transportation and storage expenses and sales of energy products.

In recent years, Energy Transfer LP has participated in several important development projects, one of which is the completion of the Dakota Access pipeline. This project was announced to the public in 2014 and completed in 2017, with a total cost of 3.78 billion US dollars. This project enhances the company's ability to transport crude oil from Bakken formation to major refining markets and provides a possible safer and more reliable choice for crude oil transportation. With the continuous development of energy industry, Energy Transfer LP has placed a strong emphasis on environmental protection and social responsibility. The company has implemented various measures to reduce its carbon footprint, including investing in renewable energy projects and adopting cleaner technologies in its operations. The survey shows that the company's stock has a high reputation in the financial market, and its share price also rises with the company's operation. Many investors are attracted and are evaluating the performance of Energy Transfer LP. The purpose of this article is to make a comprehensive financial analysis of the company and to help stock investors make better decisions.

2. Performance Evaluation

2.1. Liquidity

Table 1: The liquidity ratios of Energy Transfer LP and its competitors in 2023.

Company names	Current ratio	Quick ratio	Cash ratio
Energy Transfer LP	1.1025	0.8828	0.0143
Kinder Morgan Inc.	0.3520	0.2793	0.0133
Enbridge Inc.	0.8259	0.7410	0.3433
Williams Company Inc.	0.7741	0.7271	0.3688

Data Source: Nasdaq

Table 2: The liquidity ratios of Energy Transfer LP from 2021 to 2023.

Year	Current ratio	Quick ratio	Cash ratio
2021	0.9725	0.7866	0.0310
2022	1.1652	0.9278	0.0247
2023	1.1025	0.8828	0.0142

Data Source: Nasdaq

When considering investing in Energy Transfer stocks, it is essential to evaluate its liquidity performance, including Current ratio, Quick ratio, and Cash ratio, because those ratios reflect the company's ability to repay short-term debts and the proportion of current assets to all assets [4]. In addition to comparing the ratio of Energy Transfer LP with that of its competitors, it is necessary to analyze it with its own historical data to discover the development trend of the company.

As Table 1 shown, Energy Transfer LP’s current ratio ranked the highest among the four companies in 2023, which is 1.1025. According to market standards, if a company's current ratio is

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greater than one, it means that it is considered less risky, because the company can more easily liquidate its current assets to repay short-term debts. The asset liquidity of Energy Transfer LP is competitive, and it has the strongest ability to repay short-term debts. This can show that the financial risk faced by Energy Transfer LP is smaller than that of other companies, because the lack of debt repayment ability will lead to the bankruptcy of the company. However, only considering this ratio may result errors in the final analysis result, because a large part of the company's current assets are inventories and account receivables that cannot be quickly liquidated.

Quick ratio can make the evaluation of liquidity more complete because its calculation eliminates the inventory contained in current assets. Although the quick ratio of Energy Transfer LP is lower than the ideal value of 1, which is 0.8828, it is still far higher than its competitors, and its ability to repay short-term debts without relying on clearing inventory is still considerable. However, the cash ratio of Energy Transfer LP is greatly inferior to that of its competitors, which reflects that the company has less cash reserves for short-term liabilities. Investors should pay extra attention to this value when considering investment, because it means that Energy Transfer LP may need to liquidate other assets to obtain additional financing when repaying debts.

Compared with the three-year liquidity ratio of Energy Transfer LP, this company has the strongest asset liquidity in 2022 (see Table 2). And its cash ratio is decreasing year by year, which reflects the gradual decrease of the company's cash ratio to total assets. However, the reduction of this ratio should not be absolutely considered negative, because it is closely related to the company's business strategy. For example, the company may use lots of cash to expand its business. Although it will bring short-term liquidity risk, it may be beneficial to the long-term development of the company.

2.2. Solvency

Table 3: The Solvency ratios of Energy Transfer LP and its competitors in 2023.

Company names	Total Debt Ratio	Long-term Debt Ratio	Times-Interest-Earned ratio
Energy Transfer LP	0.6755	0.4519	3.1711
Kinder Morgan Inc.	0.5733	0.3952	0
Enbridge Inc.	0.6592	0.4144	3.0668
Williams Company Inc.	0.7643	0.4442	4.5639

Data Source: Nasdaq

Table 4: The Solvency ratios of Energy Transfer LP from 2021 to 2023.

Year	Total Debt Ratio	Long-term Debt Ratio	Times-Interest- Earned ratio
2021	0.6972	0.4626	4.0309
2022	0.6827	0.4568	3.6331
2023	0.6755	0.4519	3.1711

Data Source: Nasdaq

The company's ability to meet its long-term obligations has also been highly valued by investors and shareholders [5]. The ratios that can show the solvency of the company include Total Debt ratio, Long-term Debt Ratio and Times-interest-earned (TIE), which can help investors better understand the position of Energy Transfer LP in the market and its financial performance.

As Table 3 shown, the total debt ratio of Energy Transfer LP in 2023 is 0.6755, which means that 67.55% of its assets are financed by debt, and this ratio is close to that of its competitors. This shows that the debt ratio of Energy Transfer LP is in the middle range in the industry, and there is no outstanding performance for the amount of its total debt. Among the four companies, Energy Transfer LP has the second highest total liabilities, which may indicate that the company is highly dependent on debt and will face some debt risks. Similarly, the long-term debt ratio of Energy Transfer LP is close to that of other companies in the market, which is 0.4519, and this ratio means that the long-term debt of this company accounts for 45% of its total assets.

The value of Times-interest-earned ratio displayed by Energy Transfer LP is very healthy, which is 3.1711. The ratio means that the pre-tax income of the company is three times of its interest expense, which shows that the company's financial performance is gratifying, and it is not under great pressure to repay debts and interests. Except Kinder Morgan Inc, all competitors of Energy Transfer LP in the natural gas market have similar Times-interest-earned ratio, which also demonstrates that the natural gas market is currently in good financial health and the industry development is worth looking forward to.

In the past three years, the Solvency ratios of Energy Transfer LP have not changed much (see Table 4). Although there are some small fluctuations, all the ratios are in the middle range. The only thing worthy of attention is that the company's Times-interest-earned ratio is in a continuous downward trend, which may be caused by the company's reduced income. But overall, Energy Transfer LP has a balanced debt ratio, and the debt does not cause great pressure on it, so it can spend more time on improving its business strategy. From the perspective of the whole market, most energy companies have similar ratios, which may prove that most companies adopt similar strategies in debt management.

2.3. Profitability

Table 5: The Profitability ratios of Energy Transfer LP and its competitors in 2023.

Company names	Profit Margin	Operating Margin	Asset Turnover
Energy Transfer LP	0.0501	0.1056	0.7439
Kinder Morgan Inc.	0.1559	0.2780	0.2188
Enbridge Inc.	0.1418	0.1982	0.2497
Williams Company Inc.	0.2915	0.3953	0.2252

Data Source: Nasdaq

Table 6: The Profitability ratios of Energy Transfer LP from 2021 to 2023.

Year	Profit Margin	Operating Margin	Asset Turnover
2021	0.0811	0.1304	0.7086
2022	0.0529	0.0861	0.8402
2023	0.0501	0.1056	0.7439

Data Source: Nasdaq

When considering investing in a company's stock, it is essential to analyze its profitability, because it can understand the profitability performance of Energy Transfer LP and find its potential strategic improvement through its profit margin, operating margin, and asset turnover.

In 2023, the profit margin of Energy Transfer LP is the lowest among the four companies as shown in Table 5. Its profit margin is only 5.01%, which shows that only 5 cents of its income per dollar can be converted into net income. Its competitors have much higher profit margin than it, and the highest Williams Company Inc even reached 29.15%. The low profit margin of Energy Transfer LP indicates that it may have problems in cost management or pricing, and it has huge room for improvement. Similarly, the Operating margin of Energy Transfer LP is much lower than that of its peers, accounting for 10.56%. Williams Company Inc has the highest Operating Margin and its margin four times that of Energy Transfer LP. The relatively low operating margin reflects that Energy Transfer LP may have higher operating costs, or its competitors may have better operating efficiency.

However, the asset turnover rate of Energy Transfer LP is the highest among the four companies, reaching 74.39%. This value is in sharp contrast with its performance on profit margin and operating margin. This ratio shows the positive operational capability of Energy Transfer and proves that the company can effectively use assets to support its product sales and generate income from assets.

According to the data of the past three years, Energy Transfer LP has not made a big improvement in profitability (see Table 6). From its profitability ratios, the company can focus on enhancing cost control and the transformation of net income to increase revenue and show stronger profitability.

3. Valuation

3.1. Forecast

Table 7: Forecast of Energy Transfer LP and its competitors.

Company Name	ENB	KMI	ET	WMB
Share Price (21-Mar-24)	$35.79	$18.11	$15.59	$38.43
TTM EPS	2.07	1.07	1.09	1.91
NTM EPS	2.05	1.22	1.45	1.82
EPS growth rate	-0.97%	14.02%	33.03%	-4.71%
Revenue growth rate	-1.33%	15.03%	10.05%	1.05%
TTM P/E ratio	17.29	16.93	14.30	20.12
NTM P/E ratio	17.46	14.84	10.75	21.12
PEG	-17.90	1.21	0.43	-4.27
GP/A (based on the most fiscal year)	12.36%	10.69%	9.54%	13.09%
Profitability ratio (based on the most fiscal year)	0.24	0.22	0.69	0.21
Gross Margin ratio (based on the most fiscal year)	0.51	0.49	0.23	0.63

Data Source: Nasdaq & Estimize

Through price comparison, it is easy to find that the current share price of Energy Transfer LP is lower than its competitors, especially far lower than Enbridge Inc. and Williams Company, which is only half of their share price (see Table 7). The lower stock price can be considered that the investment barrier of this stock is not high, and it will not cause great economic pressure to investors who want to buy this stock in large quantities. The TTM EPS and NTM EPS exhibited by these four companies all show that there is little difference in stock returns in the natural gas market, which may be because the impact on the stock prices of energy companies is more from the external environment. An outstanding figure is the growth rate of earnings per share of Energy Transfer, which is 33.03%, and it is far greater than its competitors. The remarkable EPS growth rate of Energy Transfer stock may attract growth-oriented investors [6].

However, although the stock of Energy Transfer LP has its unique competitive date, investors still need to pay attention to all its ratios. It is worth mentioning that the Gross Margin of this stock is the lowest among the four companies and far below its competitors. Gross Margin represents the percentage of the company's net income in Revenue after deducting the Cost of Goods Sold. The Gross Margin ratio of Energy Transfer LP is 0.23, which means that the company can only keep 0.23 dollars in every dollar of its income. Low gross margin ratio often represents the company has problem in cost management. Investors should carefully consider the impact of this ratio before investing, because it may be a harbinger of potential problems, and low net income may affect the long-term development of the company, such as expansion. In contrast, the competitors of Energy Transfer LP can control the Gross Margin ratio at about 0.5, and the difference may indicate that the operation of Energy Transfer LP may be different from its peers in labor cost and raw material selection.

Regarding the estimation of future prices, the NTM P/E ratio exhibited by Energy Transfer shows a downward trend, and its P/E ratio is the lowest among the four companies. Low P/E ratio generally indicates that the company's share price is undervalued compared with its income, and investors' expectations for the future growth of the company's share price are relatively low. In addition, the low P/E ratio may also be closely related to the emergence of new energy sources. At present, many energy users prefer to use products driven by new energy, such as new energy vehicles that consume electricity, because it is cheaper and more environmentally friendly [7]. Therefore, investors' expectations for the natural gas market have decreased, and the P/E ratio of the whole industry is declining.

For investors who are considering buying shares of Energy Transfer LP, this stock has its investment advantages, but it also has certain risks. Before investing, investors must consider whether the return they can get is greater than these risks, and whether they are willing to bear the losses caused by risks. From an optimistic point of view, the high EPS growth rate of the shares of Energy Transfer LP means more potential returns, and investors can get huge benefits from this investment [8]. From a pessimistic point of view, the inferior ratio of Energy Transfer LP means that there are problems in the company's operational efficiency, which may lead to the company's future development becoming worrying.

3.2. Risks and Strategy

Environmental concern will be a risk for the natural gas industry. With the public paying more and more attention to the environment and reducing pollution, natural gas companies will face potential restrictions, increased costs, and damaged reputation. Because although natural gas is considered as a substitute for coal and oil, the production and use of natural gas will still lead to a large number of greenhouse gas emissions, and which will lead to more serious water pollution and habitat destruction. Therefore, in the future, consumers may object to the use of natural gas, or natural gas companies will invest money to reduce emissions.

Changing policies will also be a risk for the natural gas industry because it may lead to rising costs and fines. Policy restrictions will cause natural gas companies to spend extra money and energy on controlling emissions and complying with regulations, which will lead to a substantial increase in costs. Because if the company's current technology can't support its emissions to stay within the prescribed range, it will have to reduce production or buy and develop new technologies. In addition, the political situation and environmental problems will also affect the operation and consumption of natural gas. Natural gas companies need to continue to pay attention to the current economic and political situation and make corresponding adjustments, otherwise they may face losses and fines.

Technological change will also be a risk for the natural gas industry because consumers' demand for natural gas will be reduced with the emergence of renewable energy [9]. With the development of technology, the production cost of renewable energy such as solar energy and wind energy has been greatly reduced, and their production efficiency may also exceed that of natural gas in the future. Therefore, the long-term viability of natural gas companies may be at risk because of technological changes, and their profitability will also decline.

Strategically, Energy Transfer LP should focus on cost control and optimization because its GP/A ratio and Gross Margin ratio are the lowest among its competitors. The cost mainly comes from labor cost and production cost, so the optimization can be completed by adjusting the internal operation structure and products. For the internal structure, Energy Transfer LP should conduct a complete investigation on its expenditure on labor, then find out unnecessary projects and reduce the expenditure on investment. In addition, Energy Transfer LP can also find ways to understand the operation mode of peers, change part of its human structure, and make the company's operation more efficient. For products, the company can make additional investment in products with higher yield ratio, or withdraw funds from projects with poor performance, so that the profitability of products can be further increased [10].

4. Conclusion

Generally speaking, the stock of Energy Transfer LP has great potential, and it has a considerable rate of return. According to the data of the past few years, the performance of this stock is stable, and the operation of the company has not experienced great fluctuations. Through the analysis of stock data, it can still see that there are some risks in this stock, and these may come from the company's operation structure. If the company can make some strategies to improve this, this stock will be more attractive to financial investors. In addition, a large part of the stock risk of energy companies comes from the external environment, such as people's attitude towards energy companies. Therefore, before investing, investors need to make some investigations on the natural gas market to ensure whether the development trend of this industry is stable in the next few years.

Moreover, while Energy Transfer LP demonstrates stability and potential for favorable returns, the analysis also highlights underlying risks stemming from its operational framework. Addressing these risks through strategic initiatives could enhance the stock's appeal to financial investors. Additionally, it's crucial to acknowledge the significant influence of external factors, particularly public perception towards energy companies, which can significantly impact stock performance. Therefore, prospective investors are advised to conduct thorough assessments of the natural gas market to ascertain the industry's developmental trajectory in the forthcoming years. By integrating these insights into their investment strategies, investors can better position themselves to capitalize on the opportunities presented by Energy Transfer LP and navigate the potential challenges inherent in the energy sector.

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