

Spire Inc

Moving to the Sidelines on Negative MO Rate Case Data Points. Downgrade to Neutral

Last week, the MoPSC issued an amended order in Spire's rate case, authorizing a slightly below-average 9.37% ROE and confirming a modified capital structure with the inclusion of short-term debt, among other elements. We see the outcome as disappointing, diverging from initial expectations for a smooth rate case process, reversing MO's improving regulatory backdrop, and ultimately reducing earnings power versus more balanced results. MO regulation remains inconsistent at best, with markedly different rate case outcomes across utilities over the past several years, and Spire's latest order amplifies untenable regulatory instability, in our view. Given SR's undetermined path forward in addressing case challenges and the STL Pipeline's uncertainty at FERC, we do not expect the rate order to serve as a clearing event and anticipate SR's current -9% discount on 2023E earnings to persist absent full clarity across consolidated earnings power. As a result, we downgrade SR to Neutral.

- Capital structure, capitalized overhead questions loom over rate order.** After several rounds of issued orders, we now estimate a ~50.5% CE layer using Spire Missouri's ending long-term debt and equity as of 5/31/21 plus assumed short-term debt ex Winter Storm Uri impacts (order specifies a 13-month average, with the corresponding value not disclosed). This short-term debt inclusion significantly lowers the utility equity layer versus SR's 54.25% ask and lands as a surprise after Staff's May testimony supported the higher equity layer, a level also consistent with SR's prior MO rate case. We see continued questions over utilizing both ending (long-term debt, equity) and average (short-term debt) figures, particularly given a long-term debt issuance at the true-up period's end potentially double counts debt. However, associated commission modifications now reduce our confidence in SR achieving reasonable future outcomes and drive a ~30c cost of capital/cap structure earnings power hit (inclusive of a lower ROE already reflected in our prior estimates). Separately, we highlight attention on PSC questions surrounding capitalized overhead accounting and the commission's intent to suspend capitalizing non-operational overhead during a broader accounting review for an unquantified, temporary earnings drag. We read the amended order's new regulatory asset language as potentially covering some of this associated EPS drag, although we look for review mechanics and forward recovery dynamics between expensed and capitalized overhead to confirm the ultimate EPS risk. Rate case expectations have been volatile of late since the MoPSC's October agenda meeting to resolve contested issues, over which the commission has published three rate orders in the review. Regulatory risk remains elevated, and any final earnings impacts may differ from these estimates, particularly where novel commission actions and ambiguous order language around overheads currently cloud what SR can book or defer from earnings. Overall, we see this regulatory instability as concerning and largely incompatible with market expectations across the sector.

Sources for: Style Exposure – J.P. Morgan Quantitative and Derivatives Strategy; all other tables are company data and J.P. Morgan estimates.

See page 5 for analyst certification and important disclosures.

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▼ Neutral

Previous: Overweight

SR, SR US

Price (15 Nov 21): \$63.61

▼ **Price Target (Dec-22): \$70.00**
Prior (Dec-22): \$76.00

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J.P. Morgan Securities LLC

Key Changes (FYE Sep)

	Prev	Cur
Adj. EPS - 22E (\$)	4.41	4.25

Quarterly Forecasts (FYE Sep)

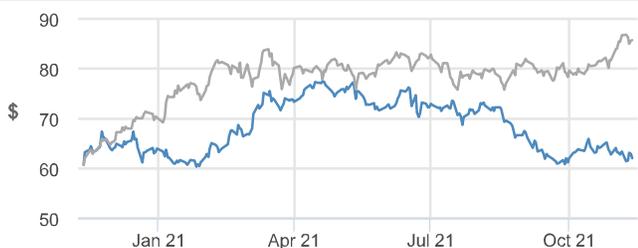
Adj. EPS (\$)	2020A	2021E	2022E
Q1	1.33	1.42A	
Q2	2.74	3.71A	
Q3	0.07	0.06A	
Q4	(0.37)	(0.67)	
FY	3.76	4.51	4.25

Style Exposure

Quant Factors	Current %Rank	Hist %Rank (1=Top)			
		6M	1Y	3Y	5Y
Value	8	18	16	32	24
Growth	12	12	51	33	97
Momentum	81	60	85	65	70
Quality	18	52	72	56	45
Low Vol	60	47	41	49	5
ESGQ	75	25	99	85	-



Price Performance



	YTD	1m	3m	12m
Abs	-3.2%	-3.2%	-13.4%	2.1%
Rel	-25.3%	-11.2%	-20.8%	-39.1%

Company Data

Shares O/S (mn)	52
52-week range (\$)	77.95-59.29
Market cap (\$ mn)	3,282.28
Exchange rate	1.00
Free float(%)	97.0%
3M - Avg daily vol (mn)	0.32
3M - Avg daily val (\$ mn)	20.4
Volatility (90 Day)	22
Index	RUSSELL 2000
BBG BUY HOLD SELL	6 4 0

Key Metrics (FYE Sep)

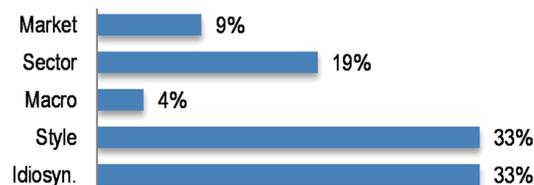
\$ in millions	FY20A	FY21E	FY22E	FY23E
Financial Estimates				
Revenue	1,855	2,162	1,736	1,777
Adj. EBITDA	404	627	635	673
Adj. EBIT	207	417	412	442
Adj. net income	193	233	223	240
Adj. EPS	3.76	4.51	4.25	4.50
BBG EPS	3.74	4.47	4.38	4.64
Cashflow from operations	470	224	473	503
FCFF	(76)	(302)	(16)	10
Margins and Growth				
Revenue growth	(5.0%)	16.5%	(19.7%)	2.3%
EBITDA margin	21.8%	29.0%	36.6%	37.9%
EBITDA growth	(19.7%)	55.2%	1.3%	6.1%
EBIT margin	11.1%	19.3%	23.7%	24.9%
Net margin	10.4%	10.8%	12.8%	13.5%
Adj. EPS growth	0.9%	19.9%	(5.7%)	5.9%
Ratios				
Adj. tax rate	12.3%	19.5%	20.2%	20.2%
Interest cover	3.8	5.9	5.6	5.5
Net debt/Equity	1.5	1.7	1.6	1.6
Net debt/EBITDA	9.6	7.0	7.2	7.1
ROCE	2.9%	5.0%	4.6%	4.7%
ROE	7.6%	9.0%	8.2%	8.5%
Valuation				
FCFF yield	(2.3%)	(9.2%)	(0.5%)	0.3%
Dividend yield	3.9%	4.1%	4.3%	4.5%
EV/Revenue	3.7	3.4	4.4	4.4
EV/EBITDA	16.8	11.7	12.0	11.7
Adj. P/E	16.9	14.1	15.0	14.1

Summary Investment Thesis and Valuation

We see SR's MO rate case outcome as disappointing, diverging from initial expectations for a smooth rate case process, reversing MO's improving regulatory backdrop, and ultimately reducing earnings power versus more balanced results. MO regulation remains inconsistent at best, with markedly different rate case outcomes across utilities over the past several years, and Spire's latest order amplifies untenable regulatory instability, in our view. Given SR's undetermined path forward in addressing case challenges and the STL Pipeline's uncertainty at FERC, we do not expect the rate order to serve as a clearing event, and we anticipate SR's current -9% discount on 2023 earnings to persist absent full clarity across consolidated earnings power. As a result, we downgrade SR to Neutral.

We base our December 2022 price target of \$70 on a 15.6x P/E multiple applied to our 2023 EPS estimate.

Performance Drivers



Factors	6M Corr	1Y Corr
Market: MSCI US	0.10	0.31
Sect: Utilities	0.52	0.45
Ind: Utilities	0.52	0.45
Macro:		
Crude Oil	-0.05	0.14
US 10yr yield	-0.07	0.13
Economic Surprise	0.42	0.12
Quant Styles:		
Momentum	-0.40	-0.60
Value	0.38	0.54
Growth	-0.22	-0.45

Source: J.P. Morgan Quantitative and Derivatives Strategy for Performance Drivers; company data, Bloomberg Finance L.P. and J.P. Morgan estimates for all other tables. Note: Price history may not be complete or exact.

Investment Thesis, Valuation and Risks

Spire Inc (Neutral; Price Target: \$70.00)

Investment Thesis

We see SR's MO rate case outcome as disappointing, diverging from initial expectations for a smooth rate case process, reversing MO's improving regulatory backdrop, and ultimately reducing earnings power versus more balanced results. MO regulation remains inconsistent at best, with markedly different rate case outcomes across utilities over the past several years, and Spire's latest order amplifies untenable regulatory instability, in our view. Given SR's undetermined path forward in addressing case challenges and the STL Pipeline's uncertainty at FERC, we do not expect the rate order to serve as a clearing event, and we anticipate SR's current -9% discount on 2023 earnings to persist absent full clarity across consolidated earnings power. As a result, we downgrade SR to Neutral.

Valuation

We lower our December 2022 price target to \$70/share, from prior \$76. We base our price target on a P/E multiple of 15.6x applied to our 2023 EPS estimate. The multiple incorporates a discount to the gas utility peer group, reflecting MO regulatory risk. The lower price target is in part due to decreased estimates.

Risks to Rating and Price Target

- Given the importance of capital spending levels to the company's adjusted net income, timely rate relief is a necessity for the company to continue to grow earnings. Any change to the regulatory environments may cause future earnings to materially differ from current expectations.
- Utilities are subject to federal and state regulation, including determination of allowed revenues. A meaningful change to the regulatory environment may cause future earnings to be lower than our current expectations.

Spire Inc: Summary of Financials

Income Statement - Annual						Income Statement - Quarterly												
	FY19A	FY20A	FY21E	FY22E	FY23E	1Q21A	2Q21A	3Q21A	4Q21E									
Revenue	1,952	1,855	2,162	1,736	1,777	Revenue	513A	1,105A	328A	217								
COGS	(887)	(696)	(940)	(539)	(539)	COGS	(181A)	(619A)	(97A)	(43)								
Gross profit	1,066	1,159	1,222	1,197	1,237	Gross profit	331A	486A	231A	174								
SG&A	(563)	(756)	(596)	(562)	(564)	SG&A	(143A)	(175A)	(146A)	(132)								
Adj. EBITDA	503	404	627	635	673	Adj. EBITDA	188A	311A	85A	43								
D&A	(179)	(197)	(210)	(223)	(232)	D&A	(51A)	(52A)	(53A)	(54)								
Adj. EBIT	324	207	417	412	442	Adj. EBIT	137A	259A	32A	(12)								
Net Interest	(104)	(106)	(106)	(114)	(122)	Net Interest	(26A)	(26A)	(27A)	(27)								
Adj. PBT	219	101	311	298	320	Adj. PBT	112A	233A	5A	(39)								
Tax	(35)	(12)	(61)	(60)	(65)	Tax	(23A)	(46A)	0A	8								
Minority Interest	-	-	-	-	-	Minority Interest	-	-	-	-								
Adj. Net Income	189	193	233	223	240	Adj. Net Income	73A	192A	3A	(35)								
Reported EPS	3.73	3.76	4.51	4.25	4.50	Reported EPS	1.42A	3.71A	0.06A	(0.67)								
Adj. EPS	3.73	3.76	4.51	4.25	4.50	Adj. EPS	1.42A	3.71A	0.06A	(0.67)								
DPS	2.37	2.49	2.60	2.74	2.88	DPS	0.65A	0.65A	0.65A	0.65								
Payout ratio	63.6%	66.2%	57.7%	64.4%	63.9%	Payout ratio	45.9%A	17.5%A	1084.0%A	NM								
Shares outstanding	51	51	52	52	53	Shares outstanding	52A	52A	52A	52								
Balance Sheet & Cash Flow Statement						Ratio Analysis												
	FY19A	FY20A	FY21E	FY22E	FY23E		FY19A	FY20A	FY21E	FY22E	FY23E		FY19A	FY20A	FY21E	FY22E	FY23E	
Cash and cash equivalents	6	4	0	0	0	Gross margin	54.6%	62.5%	56.5%	68.9%	69.6%	EBITDA margin	25.8%	21.8%	29.0%	36.6%	37.9%	
Accounts receivable	290	253	502	502	502	EBIT margin	16.6%	11.1%	19.3%	23.7%	24.9%	Net profit margin	9.7%	10.4%	10.8%	12.8%	13.5%	
Other current assets	319	333	380	409	438	ROE	7.9%	7.6%	9.0%	8.2%	8.5%	ROA	2.6%	2.4%	2.7%	2.4%	2.5%	
Current assets	615	591	882	911	940	ROCE	4.7%	2.9%	5.0%	4.6%	4.7%	SG&A/Sales	28.8%	40.7%	27.6%	32.4%	31.7%	
PP&E	6,074	6,356	6,742	7,099	7,457	Net debt/equity	1.4	1.5	1.7	1.6	1.6	P/E (x)	17.1	16.9	14.1	15.0	14.1	
Other non current assets	931	1,295	1,347	1,352	1,356	P/BV (x)	-	-	-	-	-	EV/EBITDA (x)	12.9	16.8	11.7	12.0	11.7	
Total assets	7,619	8,241	8,971	9,362	9,754	Dividend Yield	3.7%	3.9%	4.1%	4.3%	4.5%	Sales/Assets (x)	0.3	0.2	0.3	0.2	0.2	
Short term borrowings	1,469	1,449	1,333	1,461	1,503	Interest cover (x)	4.8	3.8	5.9	5.6	5.5	Operating leverage	(2038.7%)	728.0%	615.6%	5.7%	305.4%	
Payables	-	-	-	-	-	Revenue y/y Growth	(0.6%)	(5.0%)	16.5%	(19.7%)	2.3%	EBITDA y/y Growth	11.0%	(19.7%)	55.2%	1.3%	6.1%	
Other short term liabilities	0	0	0	0	0	Tax rate	15.7%	12.3%	19.5%	20.2%	20.2%	Adj. Net Income y/y Growth	3.1%	1.8%	20.9%	(4.4%)	7.8%	
Current liabilities	1,469	1,449	1,333	1,461	1,503	EPS y/y Growth	0.1%	0.9%	19.9%	(5.7%)	5.9%	DPS y/y Growth	5.3%	5.1%	4.4%	5.4%	5.0%	
Long-term debt	2,083	2,424	3,055	3,115	3,275													
Other long term liabilities	1,521	1,843	1,948	2,008	2,073													
Total liabilities	5,073	5,716	6,336	6,584	6,850													
Shareholders' equity	2,546	2,526	2,635	2,778	2,903													
Minority interests	-	-	-	-	-													
Total liabilities & equity	7,619	8,241	8,971	9,362	9,754													
BVPS	-	-	-	-	-													
y/y Growth	-	-	-	-	-													
Net debt/(cash)	3,546	3,869	4,388	4,575	4,778													
Cash flow from operating activities	451	470	224	473	503													
o/w Depreciation & amortization	182	197	210	223	232													
o/w Changes in working capital	57	18	(302)	(29)	(30)													
Cash flow from investing activities	(838)	(632)	(609)	(580)	(590)													
o/w Capital expenditure	(823)	(638)	(611)	(580)	(590)													
as % of sales	42.2%	34.4%	28.2%	33.4%	33.2%													
Cash flow from financing activities	372	160	229	(20)	45													
o/w Dividends paid	(122)	(143)	(144)	(143)	(153)													
o/w Net debt issued/(repaid)	236	268	387	60	160													
Net change in cash	(16)	(2)	(156)	(127)	(42)													
Adj. Free cash flow to firm	(284)	(76)	(302)	(16)	10													
y/y Growth	(782.0%)	(73.3%)	297.3%	(94.6%)	(162.4%)													

Source: Company reports and J.P. Morgan estimates.

Note: \$ in millions (except per-share data). Fiscal year ends Sep. o/w - out of which

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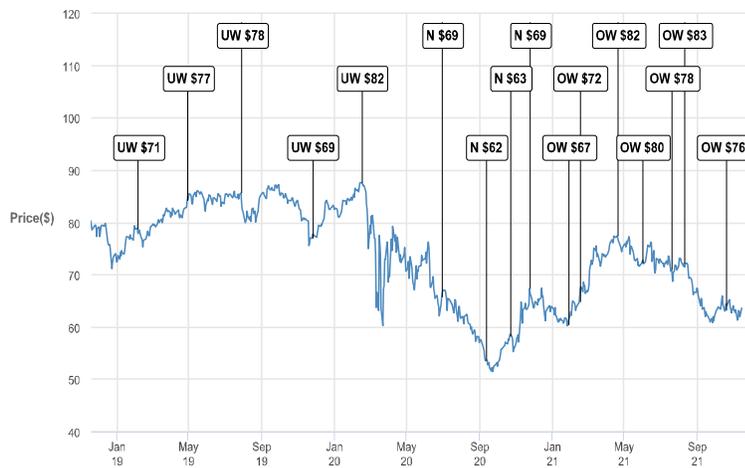
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North America Equity Research
16 November 2021

J.P.Morgan

Spire Inc (SR, SR US) Price Chart



Date	Rating	Price (\$)	Price Target (\$)
06-Feb-19	UW	78.76	71
01-May-19	UW	84.19	77
30-Jul-19	UW	85.69	78
26-Nov-19	UW	76.93	69
17-Feb-20	UW	87.58	82
01-Jul-20	N	65.71	69
13-Sep-20	N	53.57	62
23-Oct-20	N	58.26	63
25-Nov-20	N	67.36	69
29-Jan-21	OW	60.46	67
17-Feb-21	OW	64.81	72
22-Apr-21	OW	77.38	82
02-Jun-21	OW	72.20	80
21-Jul-21	OW	71.00	78
12-Aug-21	OW	72.20	83
20-Oct-21	OW	63.22	76

Source: Bloomberg Finance L.P. and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Aug 20, 2013. All share prices are as of market close on the previous business day.

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
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IB clients**	54%	49%	35%
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IB clients**	78%	71%	52%

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North America Equity Research
16 November 2021

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