CPMT
Calgary Portfolio Management Trust

Enterprise Products Partners

Energy
NYSE: EPD
Market Outperform | Buy

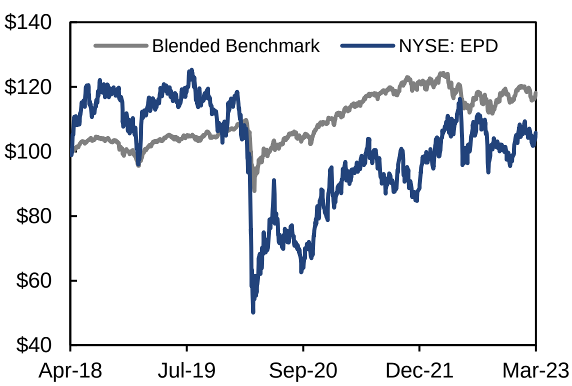
March 31, 2023
Ryan Crisalli, Investment Analyst

Return on Investment	
Current Share Price	$25.53
Intrinsic Value	$30.40
Dividend Yield	7.90%
Implied Discount	19%
Conviction Rating	1

Market Profile	
52-Week Range	$22.90 - $28.65
Market Capitalization (US$mm)	$55,550
Net Debt (US$mm)	$26,996
Enterprise Value (US$mm)	$82,546
Beta (5-Year Monthly)	1.05

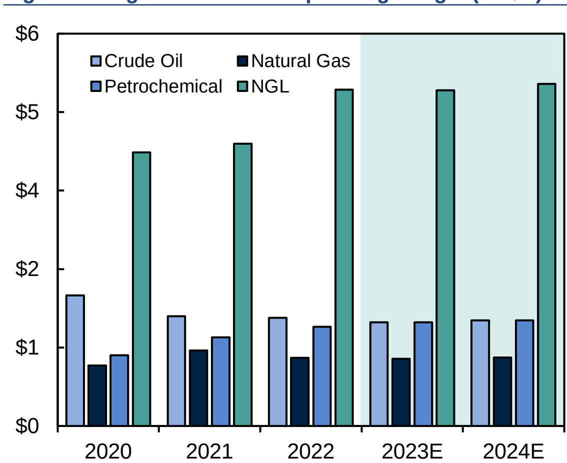
Metrics	2022A	2023E	2024E
Revenue (US$mm)	$58,186	$58,853	$60,051
GOM (US$mm)	$9,356	$9,417	$9,608
DCF/unit (US$)	$3.52	$3.53	$3.62
EV/EBITDA	9.2x	9.0x	8.7x

Historical Trading Performance (Indexed to $100)



Source: S&P Capital IQ

Figure 1: Segmented Gross Operating Margin (US$B)



Source: Company Filings, CPMT Estimates

Business Description

Enterprise Products Partners (NYSE: EPD) operates a fully integrated midstream network that services producers and consumers of natural gas, natural gas liquids (NGLs), crude oil, and petrochemical and refined products. EPD links energy producers from the largest U.S. basins to domestic and international markets. The Company owns ~50,000 miles of pipeline, 260mboe of liquids storage, 20 deep water docks, 29 natural gas processing plants, 25 fractionators, and two propane dehydrogenation (PDH) facilities.

Segment Overview

EPD offers a full-service asset network that can be categorized into four main product segments: (1) NGLs, (2) Crude Oil, (3) Natural Gas, and (4) Petrochemical & Refined Products.

NGLs: In its raw form, natural gas produced at the wellhead contains varying amounts of NGLs, such as ethane and propane. Natural gas streams containing NGLs and other impurities are not acceptable for transportation in downstream natural gas pipelines or for commercial use of fuel. Therefore, production must be transported processing facilities to remove these impurities. Generally, on an energy-equivalent basis, NGLs have a greater economic value as a feedstock for petrochemical production.

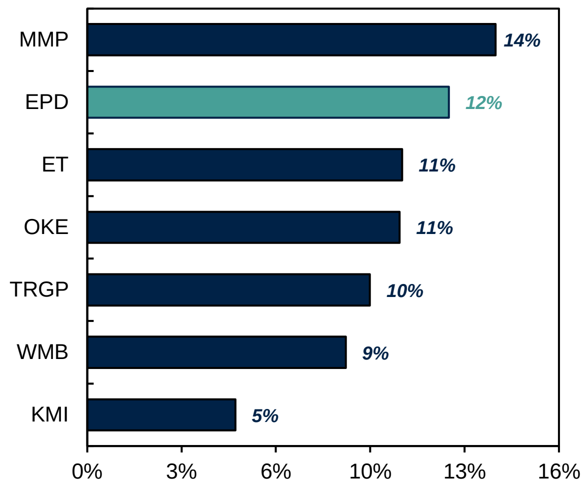
EPD operates 24 processing facilities, which run at a ~67% utilization rate and have 10.9 bcf/d of operating capacity. Contracts are either fee-based (74%) or commodity-differential based (26%). EPD markets “equity production” retained through the commodity-differential based contracts. The Company also operates NGL pipelines that transport mixed NGLs from processing facilities to downstream markets such as EPD-owned fractionators, storage, marine terminals, and third-party sites.

Crude Oil: EPD operates crude oil pipelines where it collects a transportation fee as its primary source of revenue. In aggregate, these pipelines experienced throughput volumes of 2.2 mmboe/d in 2022. The Company’s largest system is its Midland-to-ECHO system, which transports products from the prolific Permian basin to the Enterprise Crude Houston (ECHO) storage terminal. This system provides access to every refinery along the Gulf Coast. EPD also operates crude oil terminals that provide Gulf Coast refiners with an integrated system that includes supply optionality, significant storage capabilities, and high-capacity pipeline systems.

Natural Gas: The Company’s natural gas pipelines run at an average utilization rate of 65% with ~25 bcf/d of capacity. Its largest network is the Texas Interstate system which connects supply from the Permian, Eagle Ford, and Barnett basins to Gulf Coast markets.

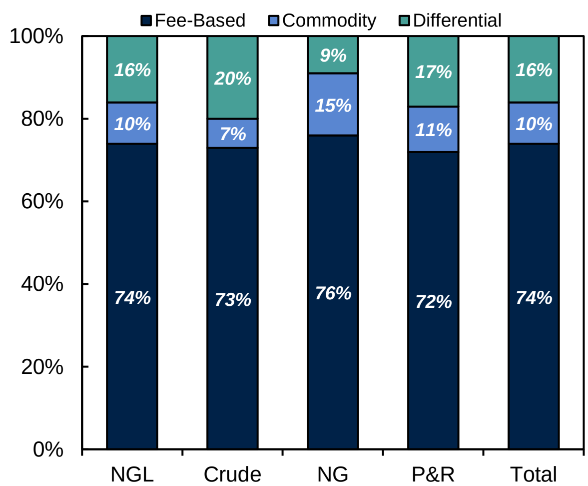
Petrochemical: EPD’s propylene fractionation units separate refinery grade propylene (RGP) into either polymer grade (PGP) or chemical grade (CGP) for resale to customers. The Company also produces “on purpose“ PGP from its PDH unit, sold to customers under long-term (take-or-pay) contracts. EPD’s Morgan’s Point Ethane Export Terminal is the largest ethane export terminal in the world, with the capacity to load 1.4 bcf of ethylene per year. EPD also operates refined product pipelines that connect into concentrated U.S. midwest manufacturing facilities.

Figure 2: ROIC vs Peers



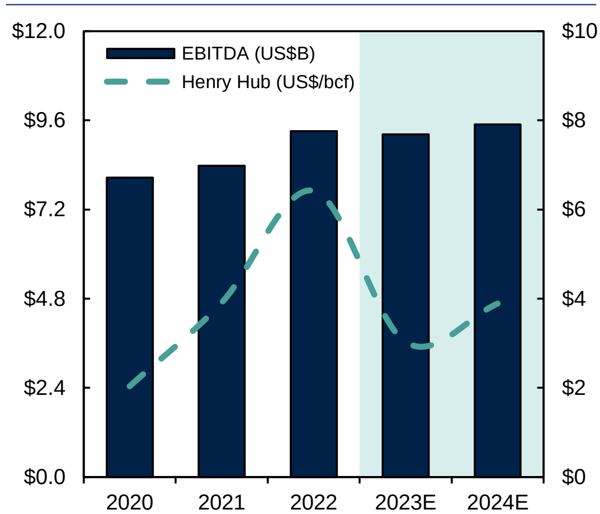
Source: S&P Capital IQ

Figure 3: Segmented Contract Breakdown



Source: S&P Capital IQ

Figure 4: LHS EBITDA vs RHS Henry Hub Spot Price



Source: CPMT Estimates, EIA, S&P Capital IQ

Industry Overview

Within the U.S. energy infrastructure industry, EPD's peer group consists of diversified midstream companies such as: Energy Transfer, Kinder Morgan, and Williams (NYSE: ET, KMI, WMB), NGL processing & services such as: companies Targa Resources and Oneok (NYSE: TRGP, OKE), and petrochemical companies such as: Magellan Midstream (NYSE: MMP). EPD holds a leading position in the NGL processing and petrochemical industries, with current market shares of 31% and 18%, respectively. Companies are highly regulated under the Federal Energy Regulation Commission, in which governing bodies set service rates charged to customers.

The NGL processing industry will continue to benefit from increased natural gas production as the push for lower carbon emission energy production continues. This will further drive the need to transport gas to processing facilities and storage terminals, which increases NGL production. Petrochemicals will increase due to demand pull from international markets for various industrial applications.

Furthermore, the U.S. is solidifying its position as a net exporter of energy products, driven by the ongoing Russian-Ukraine conflict as countries look to more secure and stable energy sources.

Mandate Fit

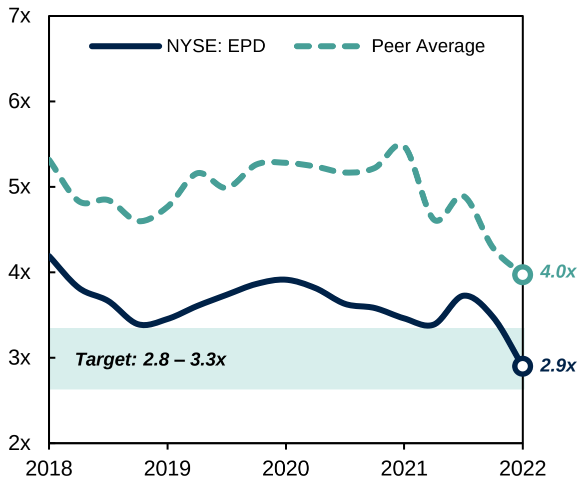
Quality Management: EPD has strategically allocated capital through project selection to ensure balance sheet protection against various product cycles. The CPMT is confident in management's ability to integrate its future growth projects into existing operations. Management continues to provide attractive unitholder returns through stable and consistently growing cash distributions and unit buybacks. Management has also established an impressive US$5.8B growth pipeline to add significant near-term operational capacity in EPD's NGL and Petrochemical segments.

Competitive Advantage: The Company has a geographical advantage through its strategically located asset network that connects every major U.S. shale basin to critical midstream and downstream infrastructure. At the core of EPD's asset portfolio is the Company's extensive NGL infrastructure, which offers deep access into key markets such as Mont Belvieu. EPD was considered a first-mover in filling the gaps in U.S. NGL infrastructure and has built out an irreplaceable system that is heavily relied upon by its customers. The Company is well positioned to capture differentials between U.S. and international markets as the U.S. shifts towards becoming a global leader in energy exports. EPD also looks to further dominate the NGL value chain through the build-out of its petrochemical segment, enabling the Company to extract higher value olefins from feedstock, creating more demand pull for domestic NGL supply.

EPD has the largest amount of NGL processing capacity in the U.S. and operates two major NGL terminals: (1) Enterprise Hydrocarbons Terminal (EHT) and (2) Morgan's Point Ethane Export Terminal. Operation of these terminals makes EPD one of the world's largest Liquefied Petroleum Gas (LPG) exporters, accounting for ~16% of global exports. EPD is also a dominant player in U.S. waterborne exports for crude oil and NGLs. The Company accounts for 22% and 33% of U.S. exports in this category, respectively.

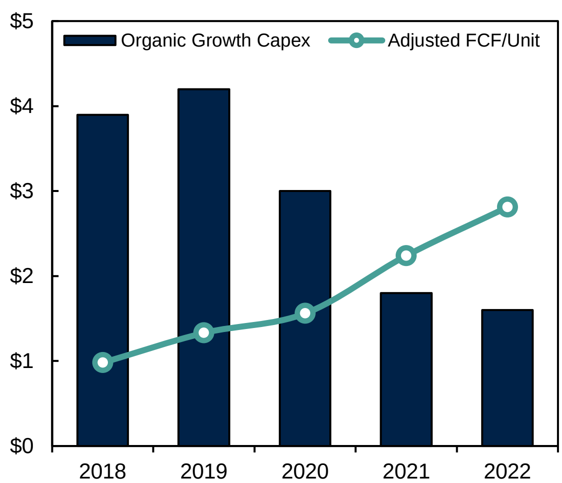
Strong Balance Sheet: EPD has a strong balance sheet exhibited through its 2.9x Net Debt/EBITDA ratio, which is well below the peer average of 4.0x. The Company has focused on reducing long-term debt through a US$1.3B decrease in 2022. This puts EPD at the lower end of its target leverage ratio range of 2.8 – 3.3x, enabling capital structure flexibility for recapitalization and the pursuit (cont.)

Figure 5: Net Debt/EBITDA vs Peers



Source: S&P Capital IQ

Figure 6: Capital Expenditure (US$B) and FCF/Unit (US$)



Source: S&P Capital IQ

of attractive growth opportunities. EPD holds investment grade ratings from Moody's (Baa), S&P Global (BBB+), and Fitch (BBB+).

Growing Free Cash Flow: EPD generated significant cash flow in 2022, representing a five-year CAGR of 23.4%, allowing the Company to make balance sheet improvements, return capital to investors, and further reinvest in core business segments. EPD's defensive characteristics allow the Company to withstand major macroeconomic events while continuing to increase its cash distributions, with a 10-year CAGR of 5.4%. EPD expects total capital expenditures in 2023 to be within the US$2.7 –2.9B range, which reflects a significant rollover from 2022. For 2023, management's focus is the integration of its current growth pipeline.

Risks

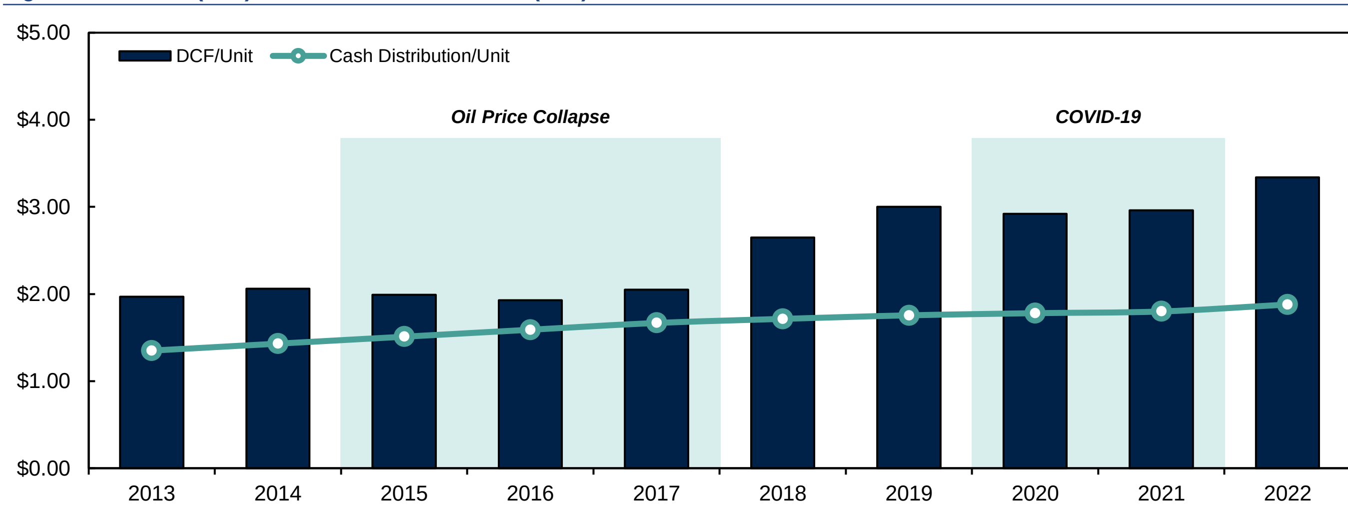
A significant risk to EPD is a potential decline in NGLs demand, given that the segment makes up over 50% of the Company's Gross Operating Margin (GOM). Similarly, any delays or reduced demand for petrochemical products (domestically or internationally from key Chinese and Indian markets) would have a significant impact on the Company's financial performance. EPD partially mitigates downside risks by contracting the long-term capacity of its facilities.

Valuation and Investment Thesis

EPD was valued at $30 using a five-year DCF with a WACC of 7.4%. The intrinsic value was derived using a 50/50 blend of (1) the Gordon Growth method, using a 0.5% terminal growth rate, and (2) an EV/EBITDA exit multiple of 9.0x. The valuation yields an implied discount of 19%.

EPD's inherent value is derived from its extensive and irreplaceable asset portfolio that is heavily depended upon by its customer base. The CPMT believes that the strategic position of its assets allows for additional benefit from increases in top U.S. oil and gas basins due to EPD's ability to access premium downstream and end-markets. The Company provides diversified cash flows through its full-service asset base, which allows for significant incremental growth opportunities. The Fund believes EPD possesses an impactful growth pipeline that can add crucial short-term capacity to key NGL and petrochemical segments.

Figure 7: DCF/Unit (US$) and Cash Distribution/Unit (US$)



Source: Company Filings