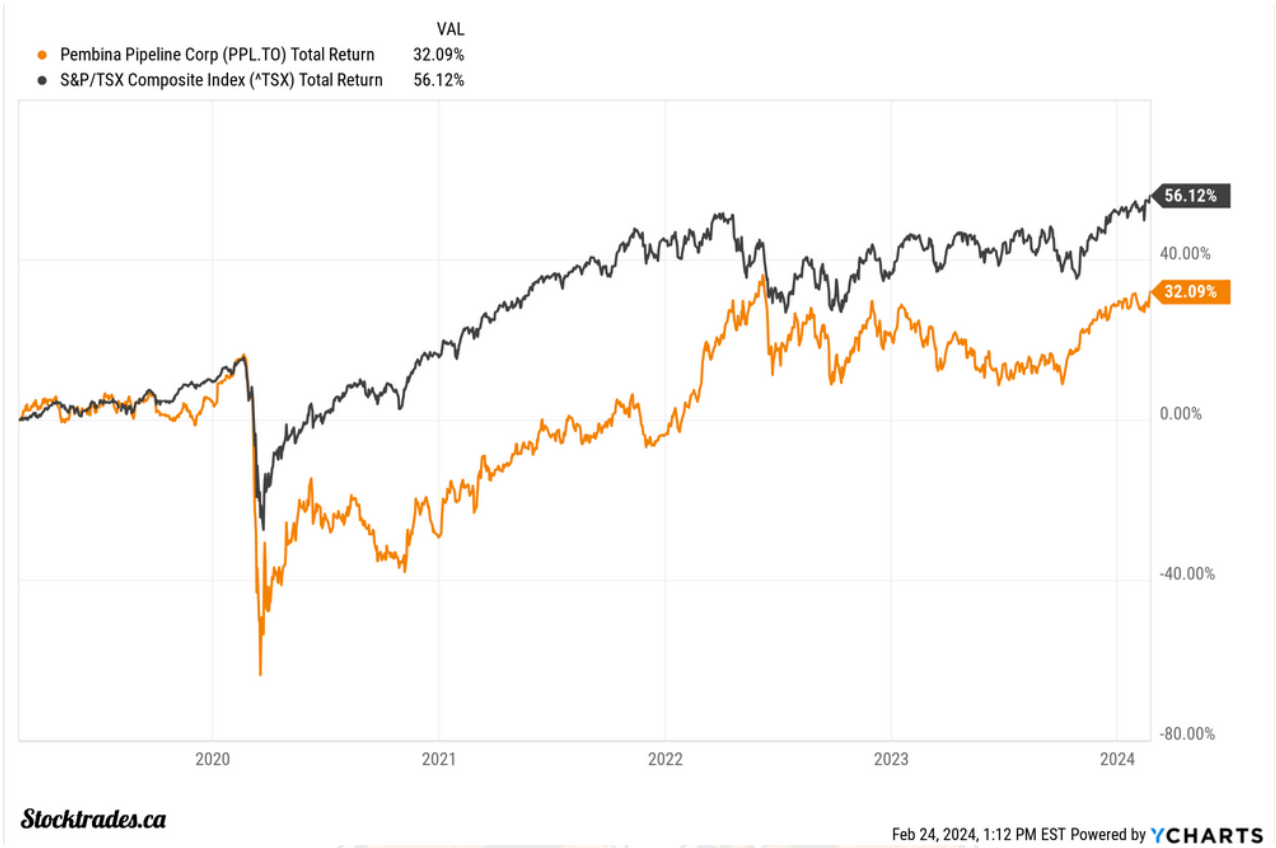
STOCKTRADES PREMIUM COMPANY SUMMARY

PEMBINA PIPELINE

PPL.TO

UPDATED FEBRUARY 24, 2024

NOTE: MAT IS LONG PPL.TO



Pembina Pipeline is a midstream company serving the Canadian and North American (primarily Bakken) markets with an integrated product portfolio. The firms' assets include pipelines and gas gathering as well as assets across fractionation, storage, and propane exports.

OUR GROWTH SCORE: 2.3/5

OUR DIVIDEND SAFETY SCORE: 2.3/5

Sector: Energy

Stock Type: Dividend/Value

Industry: Oil & Gas Midstream

Our Risk Rating*: Moderate

Current Price: $46.84

1 Year Price Target: $51.67

PROS

- Strong management and history of execution.
- One of the least leveraged companies in the industry.
- Trading at attractive valuations relative to historical average and industry peers.
- Offers an excellent and sustainable yield north of 6%.
- Financial flexibility allows it to pursue a number of potential growth opportunities.
- The company can fund increased CAPEX with internally generated cash flows
- Has been focused on de-leveraging and debt-to-EBIDTA ratio has been in a steady decline, hitting 3.3x, below the lower end of target range (3.5x)

CONS

- 10-20% of the business is exposed to commodity prices which can lead to volatility.
- While it is diversified (20 customers account for 70% of business), it is more exposed to smaller customers than its peers.
- Flat growth expected in Fiscal 2023
- Even though the company is better positioned than most and 94% of its debt is fixed rate - high-interest rates do lead to higher borrowing costs and could stunt growth in the near term.
- Alberta wildfires forced the closure of several of its assets.

OVERALL THESIS

Pembina has been one of the better-performing midstream companies over the past year. That said, the company's recent downtrend has middle of the pack year to date. We've closely watched PPL for a few months now, and we think the current dip presents an opportunity.

For starters, Pembina is one of the most reliable midstream companies. An excellent management team with a reliable track record of executing projects on budget and on time sets it apart from many of its peers.

While the company was expected to experience flat to negative growth in Fiscal 2023, it delivered record adjusted EBITDA of $3.8B, up from $3.7B in Fiscal 2022. Not only that, but it aimed to exit the year with a debt-to-adjusted EBITDA of 3.3 to 3.6x - one of the lowest in the industry. It achieved this with a ratio of 3.3x as of the end of Fiscal 2023.

Given the company's strong financial footing, it is well-positioned to pursue growth opportunities - whether in acquisition or new expansion opportunities.

Case in point, the company recently increased capital expenditure (CAPEX) guidance, and despite this, management still estimates that cash from operations will exceed CAPEX and

dividends. The flexibility to internally fund CAPEX in this environment is a desirable advantage and could lead to outperformance in a high rate environment.

Pembina is guiding to adjusted EBITDA of $3.725 to $4.025B, compared to the $3.8B it posted last year. Remember that this does not include contributions from the Alliance/Aux Sable Acquisition. This $3.1B acquisition, funded through a mix of cash, debt and a bought deal offering, is expected to close in the first half of Fiscal 2024. The deal is fairly large and is expected to add $225-250M in cash flow and be immediately accretive on a cash flow per share basis (mid, single-digit by the end of year 1). Management is expected to provide guidance updates closer to the closing date.

It is also well diversified across the various commodities (NGL, crude and natural gas), and 65-70% of its business is take-or-pay/cost-of-service contracts. In Fiscal 2024, it aims to achieve a fee-based contribution to adjusted EBITDA to the tune of 85-90%, inline with Fiscal 2023.

When you combine the company's current yield (6%+), its excellent financial position, attractive valuations, and its history of execution, Pembina is a desirable option for income investors. We feel steady or evening declining interest rates over the next couple of years will have interest rate-sensitive companies like Pembina outperforming.

POTENTIAL RISKS

Let's start with what is on top of everyone's mind: inflation and rising rates. As a high CAPEX industry, the company is exposed to rising rates. This negatively impacts borrowing costs which in turn can impact cash flows. The company has taken steps to mitigate by lowering debt, which is a key means by which the company can help reduce this risk. That said, higher borrowing costs impact the company's ability to grow and willingness to start new projects.

Speaking of CAPEX, pipeline companies run the risk of cost overruns when projects don't finish on time. We saw pandemic closures significantly impact many big projects, and even though this was an extreme event, several factors are still outside of Pembina's control.

Beta	**1.6**
Alpha	**N/A**
Our Risk Rating	**Mod***
Max Drawdown	**68.7%**

On the bright side, Pembina has an excellent track record of finishing projects on budget and on time.

As a midstream company and despite a highly contracted customer base, it is still subject to

*Our Risk Rating: Our opinion of the overall risk an investment presents. Can be shown as Defensive (DEF), Moderate (MOD), or Aggressive (AGG). By no means is this an indication of future potential gains or lower volatility.

the cyclical nature of commodity prices. In particular, volumes in a downtrend can impact those assets that don't include take-or-pay agreements. A quick refresher, a take-or-pay contract is one where the company gets paid regardless of product shipped. The company's Marketing Division (storage, terminals, hubs) is most exposed to commodity prices as it enters into contracts to buy and sell oil, condensate, and NGL, which Pembina then markets. Pembina estimates that 10-20% of its business is exposed to commodity prices.

Finally, we can't talk about pipelines without mentioning the adverse effects of oil spills. Pembina recently dealt with its own leak earlier this year when approximately 4600m3 of NGL was released from the company's Northern Pipeline. While it wasn't a major issue like some we've seen in the past, it is still expected to result in a ~$30M hit to adjusted EBITDA.

Here is a table that shows Pembina's commodity and currency risks as it relates to impact on adjusted EBITDA:

Pembina's 2023 adjusted EBITDA may be directly impacted by market-based prices as follows:

Key Variable	2023 Guidance Midpoint Assumption	Sensitivity	Impact on Adjusted EBITDA ($millions)
AECO Natural Gas (CAD/GJ)	$4.55	± $0.50	± 11[2]
Mont Belvieu Propane (USD/usg)	$0.86	± $0.10	± 37[2]
Foreign Exchange Rate (USD/CAD)	$1.36	± $0.05	± 33[2]
Pembina Share Price (CAD/share)	$44.98[1]	± $5.00	± 18

(1) *Closing share price on October 31, 2022.*

(2) *Includes the impact of Pembina's hedging program.*

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VALUATION

	TTM	5 Year Average	Industry Average
P/E	15.67	-	16.43
P/S	2.80	2.90	1.99
P/B	1.89	1.85	1.89
P/FCF	12.71	13.09	18.60
PEG Ratio (FWD)	N/A	N/A	N/A

When looking at standard valuation metrics, Pembina seems quite attractive. The company is trading at a discount to historical averages and, for the most part, is trading below many in the industry. It is worth noting that valuation remains relatively unchanged since our last report.

Another method to evaluate pipelines is to use Enterprise Value (EV) to Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA), or EV/EBITDA. With that in mind, Pembina is trading at an EV/EBITDA ratio of 11.53 after this past quarter. While this remains among the lowest among all TSX-listed midstream companies, it is still below historical averages (13.18).

This is despite Pembina having one of the highest returns on equity and invested capital among its peers. Also, the company is one of the least leveraged and is in a strong financial position. In our opinion, the company's current valuation relative to peers is unjustified. It provides an excellent alternative to some of the more well-known players.

COMPETITOR ANALYSIS

	PPL.TO	ENB.TO	TRP.TO
P/E	15.67	16.55	19.46
P/S	2.80	2.21	3.47
P/B	1.89	1.83	2.10
P/FCF	12.71	18.60	N/A

There are several well-known pipelines on the TSX. Premium members will be familiar with TC Energy (TRP) and Enbridge (ENB) as the two most prominent companies in the industry. There are also some smaller players like Keyera (KEY), but only Pembina sits comfortably in the middle. This allows the company to grow at a faster pace than the two giants and provides a greater level of safety than some of the smaller competitors.

DIVIDEND ANALYSIS

Annual Dividend	Fee-Based DCF Payout Ratio	5 Year Dividend Growth %	Dividend Growth Streak
$2.67	68.85%	4.56%	2

Pembina Pipeline used to be a Canadian Dividend Aristocrat. However, the company went through a period of stagnation between 2020 and 2021 before returning to growth last year. As you'll note, this was during COVID-19. The company had just entered into a significant acquisition (Kinder Morgan Canada and the Cochin Pipeline) a few months before the pandemic.

It was, therefore, not surprising that the company took a cautious approach. Last year, the company once again returned to dividend growth when it announced a 3.6% raise to the dividend following the creation of PGI, a joint venture between Pembina (60%) and KKR (40%). That was followed by another 2.3% raise earlier this year (Q1 of '23). Considering the company sports a 6%+ yield, you will not likely see huge dividend growth rates. But you don't necessarily need them either with that high yield.

Pembina's standard payout ratio ballooned to 128% after a quarter in which earnings took at hit on one time charges , but as a pipeline, it is best to look at cash flows. The company also has a target for the dividend to account for less than 100% of fee-based distributable cash flow (DCF). This is a specialized metric that you aren't going to find on any data platform. The good news is that Pembina does post this metric quarterly. It closed the year with a DCF ratio of only 80% and expects to exit Fiscal 2023 with a ratio in the 70-75% range - well within its target. Also worth noting, Pembina moved from a monthly to a quarterly dividend in Fiscal 2023. It announced the move in late 2022 to align its "dividend practices with the vast majority of its peers and companies within the TSX 60 Index."

RECENT EARNINGS

Earnings Estimates	2024	2025	2026
EPS	$2.79	$3.18	$3.29
Revenue	$9.27	$9.39	$9.95
EBITDA	$4.12	$4.32B	$4.33B
EBITDA Margins	44.48%	46.01%	43.57%

Pembina Pipeline reported strong third-quarter results. Earnings of $1.21 (+210%) per share beat expectations for $0.76, while revenue of 2.466B (-8.5%) topped estimates of $2.51B. Adjusted cash flow per share of $1.36 also came in strong, up by 8.8% YoY and in line with estimates.

There were quite a few business updates this quarter. Some notable highlights include Peace Phase III trending below budget. The original budget called for a capital spend of ~$530M and was previously revised downward to $475M. This quarter, management indicated that it now expects the project to cost $430M and will be completed in Q1. Notably, it's not often that major projects come in under budget in such a way, a testament to Pembina's strong team.

The company also reversed a charge on the Nipisi Pipeline as it was recently activated and signed a long-term contract. It now expects the pipeline to be fully contracted by the end of the year. Speaking of contracts, management also signed a long-term agreement with Dow Chemical to supply and transport up to 50K barrels per day of ethane.

Finally, the company announced that it would make a final decision on the Cedar LNG investment in mid Fiscal 2024 (slightly delayed from previous expectations for a decision to come in Q1).

As for the company's financial position, Pembina reported a strong balance sheet as of end of Fiscal 2023, with the ratio of debt-to-adjusted EBITDA of 3.3 times. As such, the company met guidance that previously called for a deleveraging in the 3.3-3.6x range. Management also reiterated Fiscal 2024 guidance, which called for adjusted EBITDA of $3.725 to $4.025B. Of note, this includes the big Alliance/Aux Sable acquisition. The acquisition is also expected to be leverage-neutral, meaning it won't significantly impact the company's debt profile.

All in all, Pembina continues to perform, and it is well-positioned to post outsized growth this year, especially once the big Alliance/Aux Sable acquisition closes. That deal should be immediately accretive to cash flow, and given the expected synergies, it should provide solid growth across the board.

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