the CAPITAL LIST

Capital InFocus

Dorian: Priced to Perform

11/21/2024

By Don Yocham, CFA

Elemental Energy

The rise of artificial intelligence (AI) is revolutionizing industries, driving unprecedented growth in energy consumption.

As AI adoption accelerates, particularly in data-intensive sectors like cloud computing and autonomous systems, the need for reliable and sustainable energy sources is becoming critical. **Hydrogen**, and by extension, ammonia as its carrier, offers a transformative solution to this challenge.

Ammonia, a versatile hydrogen carrier, is poised to play a pivotal role in meeting the energy needs of the AI-driven economy.

Shipping companies have a unique opportunity to bridge the gap between hydrogen producers and global. Unlike hydrogen in its gaseous form, ammonia is more stable and easier to store and transport, making it the ideal medium for hydrogen's long-haul journeys.

Regions investing heavily in AI, such as the United States, Europe, and Asia, are driving demand for clean energy sources to power data centers, AI training clusters, and robotics. Ammonia offers a scalable solution to these needs, particularly for areas with limited renewable energy capacity.

For shipping companies, this market represents a high-growth opportunity. With investments in ammonia-ready carriers and dual-purpose VLGCs, firms can position themselves at the forefront of the energy transition.

And **Dorian LPG (NYSE: LPG)** is prepared to serve that market well.

Priced to Perform

Headquartered in Stamford, Connecticut, **Dorian LPG Ltd. (NYSE: LPG)** ships liquefied petroleum gas (LPG) with its fleet of 25 very large gas carriers (VLGCs).

VLGCs ship liquified petroleum gas (LPG) like propane and butane. Transporting LPG requires only moderate pressure and ambient temperature. They do not include LNG (liquified natural gas), which involves transport at low temperatures (-162 degrees C).

The opportunity lies in converting that fleet to accommodate ammonia shipments, which is already underway.

The stock hit a peak price of $49.66 in May but has since pulled back nearly 50% on a steep decline in shipping rates for VLGCs. But those rates should reverse with the world ready to do business with the U.S. and energy sanity replacing green madness.

Those margins, plus the company's high free cash flow and a solid 16% return on capital, put the company in a great position to capitalize once shipping rates turn favorable.

Maintaining high profitability throughout its sharp stock price sell-off means the current $25 stock price represents a steep discount to its oil and gas peers.

As you'll see in this report, Dorian is priced to perform.

Let's get to it.

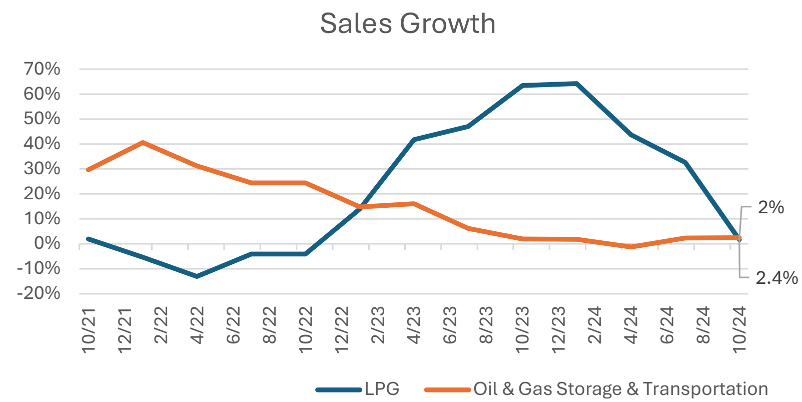
Keeping Profitability Afloat

VLGC shipping rates are down over 25% from last year.

This factor accounts Dorian's sharp revenue growth, taking it from nearly 60% annual revenue growth to in-line with the oil and gas storage and transportation market overall.

Despite the sharp revenue growth, operating profits as a percent of sales at 43% remain well above the average company in its sector.

Dorian outperforms on EBITDAR margin as well (a proxy for operating cash flow). For comparison, the average EBITDAR for S&P 500 companies is 29.2%.



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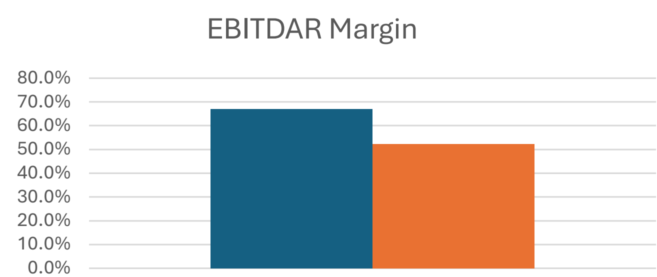

	10/31/2024
LPG	67.0%
Oil & Gas Storage & Transportation	52.4%

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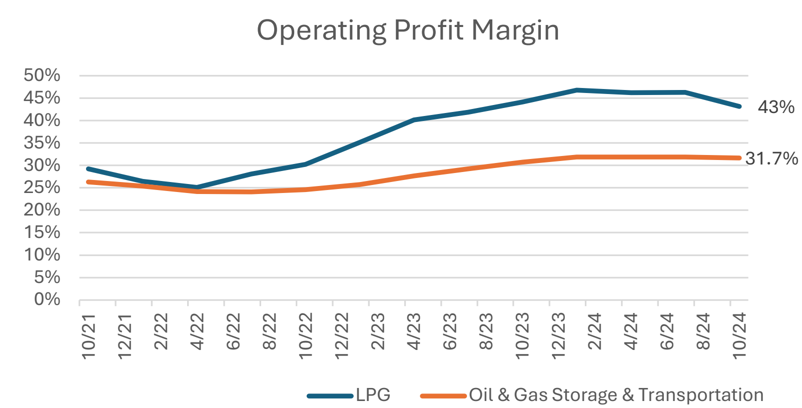

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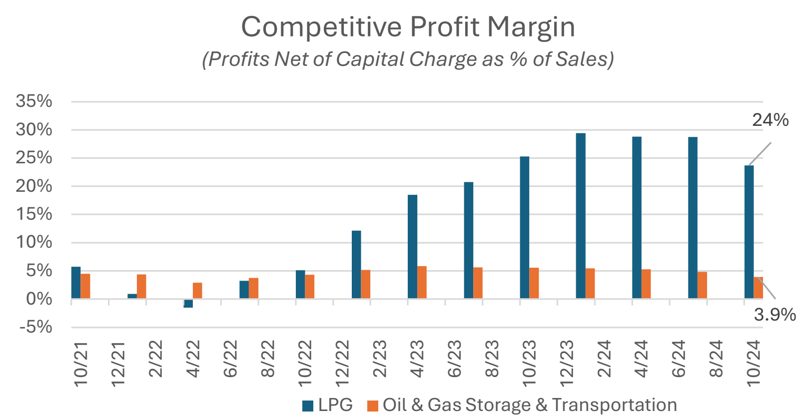
Value Add Profits and Growth

To add value and get a rising stock price over time, profits must exceed the cost of capital. That's the cost to compete. Capital costs apply to all companies, depending mostly on debt service costs and the riskiness of the company's stock.

After deducting the cost of capital, Dorian's competitive profits remain at a very high 24% compared to 3.9% for the O&G storage and transportation sector and 5.5 for the S&P 500.

The margin is declining (down 1% last quarter), but healthy profit margins provide plenty of cushion to ride out low shipping rates should they take longer to turn around than anticipated.

But the company's return on capital has remained high and stable throughout, hinting at management's ability to adjust to vagaries of global shipping.



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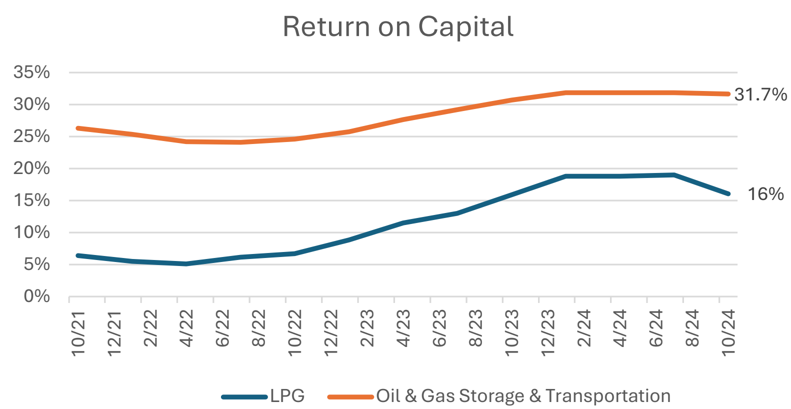

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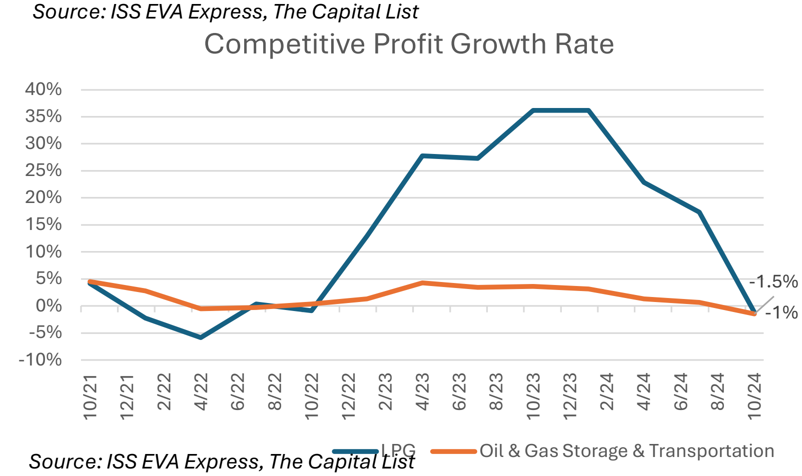

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High Quality Profits

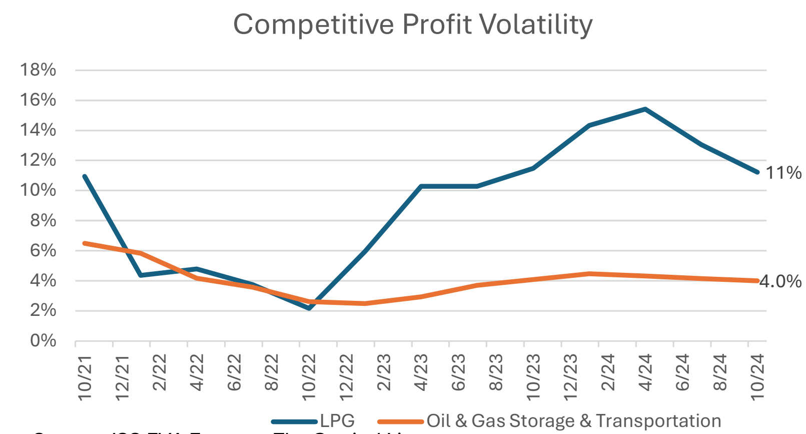
It's also important to gauge the quality of a company's competitive profits and cash flows.

Profits and cash flows are low quality when they are volatile, depend on leverage, or don't cover the capital needed to generate them.

In line with it's high return on capital, Dorian delivers very high free cash flows relative to its capital base (free cash flow spread), and carries modest debt.

Relative to the energy sector overall, its free cash flow spread is better than 88% of companies in the sector and a total debt ratio of 34.6% is a bit above average for the sector.

Profit volatility is high relative to its segment, but not so high as to cause a concern given volatile shipping rates.



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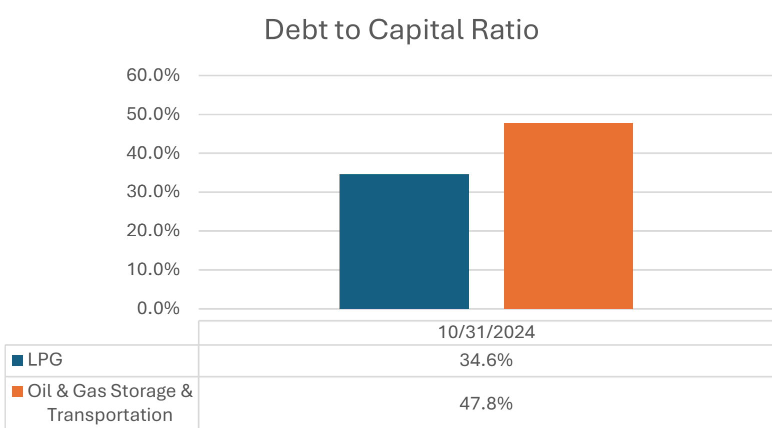

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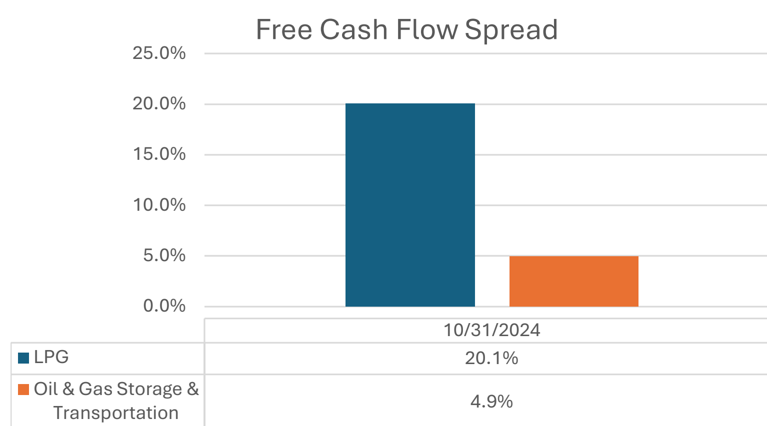

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What You Pay For

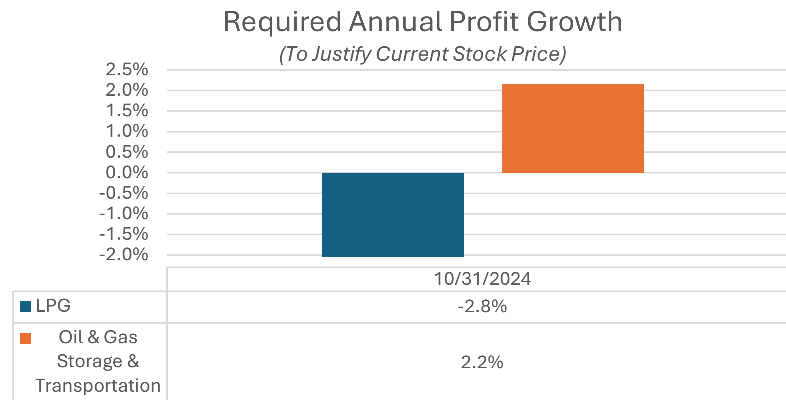
Up to this point, all of the data I have shown you have been strictly accounting measures. They involve corporate performance derived from income statements and balance sheets without any reference to the company's stock price.

Now we take a look how much you're paying to own these results.

At roughly $25 per share, the present value of Dorian's profits exceed the market cap of the stock. In other words, profits must DECLINE 2.8% to justify its price. The stock price assumes no growth in profits, contributing to Dorian's attractive valuation.

To look at it another way, the market is discounting Dorian's future profitability by 83.8%, which I consider to be a sharp overreaction to declining shipping rates.

It's operating profit multiple also screams value in light of the companies historically strong fundamentals.



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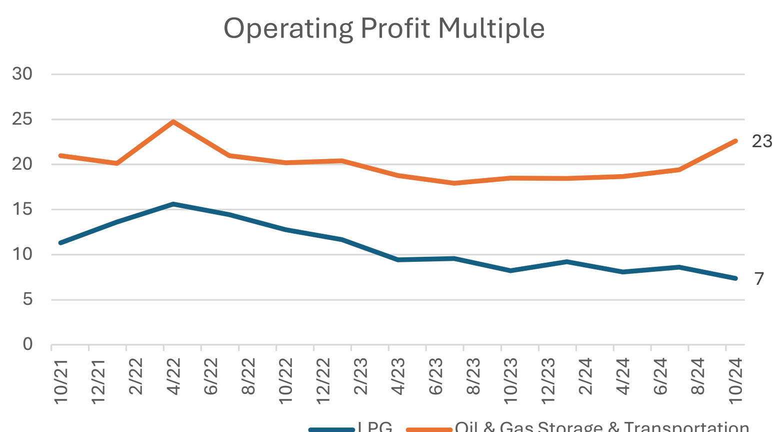

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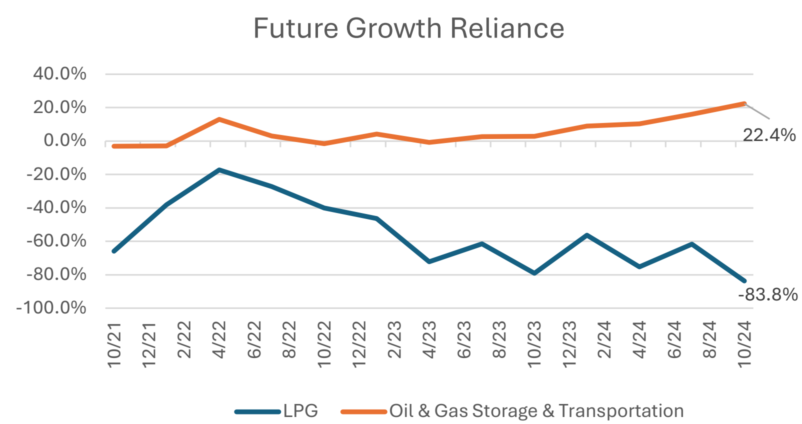

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Price Compared to Consensus

Consensus estimates have sales declining 13% over the next 5 years to $437 million.

That's in line with what sales have to be to justify its current $25 stock price, assuming it can maintain current profit margins.

So, at the very least, the stock is fairly priced

But I see a different path.

The "uncertainty meter" went way down after the recent election.

Global hot spots like Ukraine and the Middle East could find swift resolution in the coming months. Iran has agreed to stop enriching uranium to weapons grade.

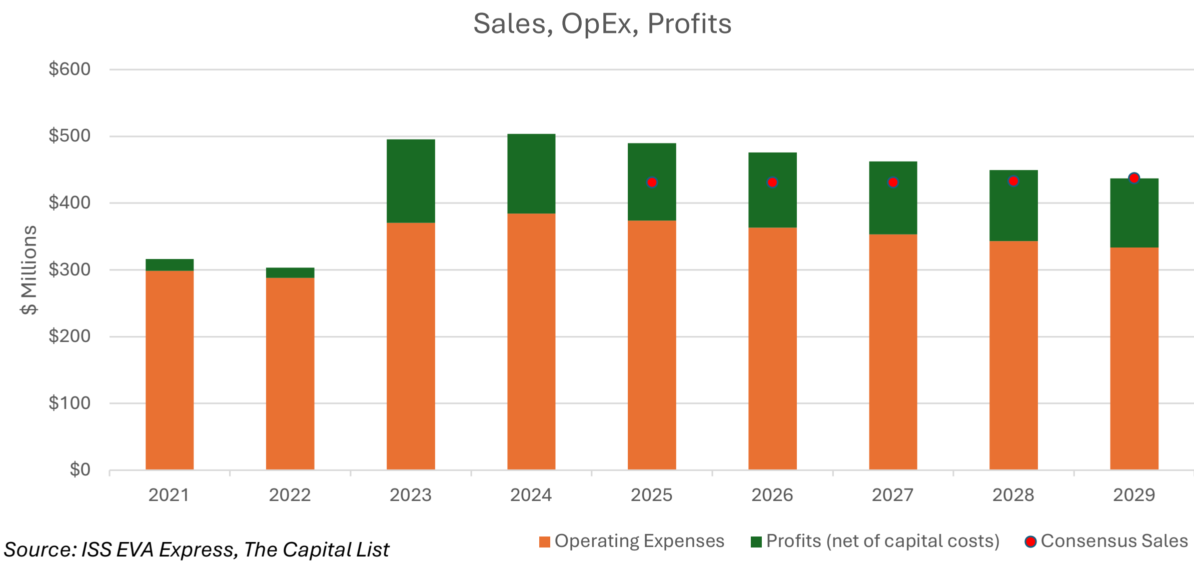
And representatives from around the world are looking to solidify trade deals with the U.S. to avoid tariffs, including boosting energy imports.

Shipping rates will rise and so will Dorian's revenue and stock price. And transporting elemental energy will boost those expected gains further.

With those two tailwinds, I expect the stock will rise to $37 over the next year.

Think Free, Be Free

Don Yocham, CFA



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