Stocks within *Value Line's* Natural Gas Utility Industry have risen some in value since our last report in February. We believe that stems partially from expectations of improved earnings this year and company-specific developments. Better-performing financial markets have also helped. Even so, the primary attraction here is these equities' reliable, healthy amounts of dividend income (which are adequately covered by corporate earnings). Moreover, at recent quotations, 3- to 5-year capital appreciation possibilities for some of the stocks in this group appear decent, resulting in solid total return potential.

INDUSTRY TIMELINESS: 37 (of 93)

Rate Filings

Rate cases are a very important factor for natural gas utilities. Federal authorities establish wholesale service tariffs, and state regulators determine retail distribution rates. Sufficient returns on common equity are necessary to keep these businesses viable. Higher rates are sought to pay for such key items as the cost of expansion, storm damage, and/or to cover the expenses of maintaining reliable service. In order to promote healthy relationships with customers and regulators, managements endeavor to keep operating and service costs as low as possible. At times, however, political pressure can compel authorities to limit rates of return, to the detriment of utility companies. But for the most part, regulators desire to strike an equitable balance between the interests of shareholders and customers. Notably, through the first half of fiscal 2024 (year ends September 30th), *Atmos Energy Corporation*, one of the more active rate-filers in our group, managed to complete some regulatory proceedings resulting in a $138.4 million increase in annual operating income. What's more, there were ratemaking initiatives in progress at the conclusion of that period seeking $96.4 million of annual operating income. (Of course, there are no guarantees that the company will get everything it wants.) When the regulatory environment is fairly quiet, utilities may place greater emphasis on expense-reduction measures and nonregulated operations (see below).

Nonregulated Units

Some industry participants have dedicated substantial resources to the nonregulated arena, which includes pipelines and energy marketing & trading services, and we see this trend continuing in the future. Indeed, these businesses offer opportunities for utilities to diversify their revenue streams. Also, the fact that nonregulated segments can provide potential upside to earnings per share is notable, since the return on equity is limited by the regulatory state commissions (generally in the 9%-11% range) on the regulated divisions.

Business Moves

Several months ago, *Chesapeake Utilities* paid NextEra Energy nearly $923 million for Florida City Gas (FCG), which serves around 120,000 residential and commercial customers across eight counties in Florida, including Palm Beach, Broward, and Miami-Dade. We like the acquisition partly because it more than doubled the natural gas operations in The Sunshine State, which has bright expansion projects. Another positive is enhanced economies of scale. Leadership adds that FCG was financed via a balanced mix of equity and long-term debt, thus maintaining the company's sound balance sheet. Elsewhere, *Southwest Gas Holdings* completed its initial public offering of Centuri Group, a provider of utility infrastructure services across the U.S. and Canada. (The original plan was a spin-off that would be tax free to stockholders for U.S. federal income tax purposes, but it didn't work out.) That move enables the two entities to focus better on the growth opportunities within their respective industries.

Generous Income Levels

The big draw of utility equities is their dividends, which tend to be sufficiently covered by corporate earnings. (It's important to mention that the Financial Strength ratings for more than half of the nine companies in our category are an A, and the remainder is a solid B++.) At the time of this industry report, the average yield for the group was approximately 4.1%, nearly two times the *Value Line* median of 2.1%. Standouts include *UGI Corp.*, *ONE Gas, Inc.*, *Northwest Natural Holding Co.*, and *Spire Inc.* When the financial markets experience heightened volatility, healthy dividend yields provide a measure of much-needed stability.

Conclusion

None of the equities in our Natural Gas Utility Industry are timely, right now, other than *UGI Corp*. Nonetheless, they ought to attract the attention of income-minded investors with a conservative bent, since these good-yielding issues boast high grades for Price Stability, and most are ranked 1 (Highest) or 2 (Above Average) for Safety. Consider, also, that there are some decent selections for capital gains potential for both the 18-month span and over the pull to 2027-2029. As always, our subscribers are advised to carefully examine the reports that follow before making a financial commitment.

Frederick L. Harris, III