EQT Corp

EQT buying back EQM; downgrade to UW on higher PF leverage, tight trading levels

Rating Change - Credit

12 March 2024

High Grade Credit
United States
Energy

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EQT to buy EQM in an all-stock transaction

On Monday morning, EQT Corp (EQT) announced plans to acquire Equitrans Midstream (bond ticker = EQM) in an all-stock transaction. EQM was previously spun out of EQT in 2018. The combined business is expected to have an enterprise value of >$35b and deal closing is planned for 4Q24, subject to a shareholder vote at both companies. The transaction is contingent on the FERC authorizing EQM's Mountain Valley Pipeline (MVP) project to commence service (excepted in 2Q24). Synergies are expected to be $250mm annually with visibility to achieving an incremental $175mm (annually) over time. EQM provides EQT with >2,000 miles of natural gas pipelines and access to its MVP project. EQT expects the pro-forma (PF) business to generate FY25 EBITDA of $5.5b (FY23 standalone EBITDA of $2,983mm) and free cash flow of ~$2.5b, at recent strip pricing.

Near-term deleveraging supported by asset sales

EQT plans to reduce total debt by >$5b (via $3.5b of asset sales and free cash flow) within 12-18 months post-close ($7.5b gross debt target). Debt repayment will be focused at the front-end of the maturity stack and EQT does not plan to collapse EQM's capital structure (i.e. the EQT and EQM notes will not be pari passu), at least until de-leveraging is complete. On its call, management noted that it has >2x the number of sales candidates necessary to reach its divestiture target. Separately, EQT affirmed its commitment to IG credit ratings and expects the combined business to be evaluated on a hybrid upstream / midstream ratings structure. Importantly, on Monday evening, Moody's placed EQT on outlook negative and affirmed its Baa3 rating.

Higher PF leverage & tight trading levels; downgrade to UW

We view this transaction favorably from an operational perspective as EQT should benefit from greater size & scale, asset diversification, a lower cost structure, and a more stable earnings stream. Over time, we think the PF business could operate with a lower breakeven and produce significantly higher free cash flow. Importantly, we think EQT's 12-18 months debt paydown plan is manageable if strip pricing holds, although we have concerns around the expected near-term spike in PF leverage if natural gas prices struggle to rebound off recent low prices. Nonetheless, management will need to execute its asset sales regardless of natural gas prices. Should de-leveraging be achieved, we think EQT could eventually trade through Ovintiv Inc (OVV, OW) though that is likely 12-18 months away and only signals ~10 bps of upside from current levels. In the near term, we think spreads are likely skewed wider given EQT's higher PF leverage, our outlook for soft gas prices in 1H24 and tight trading levels (~30-45 bps inside Enlink Midstream (ENLK), recently upgraded to investment grade, and Southwestern Energy (SWN) a rising star to IG at the agencies). We also note that EQT's outperformance on Monday was due to short covering (EQT was one of the top shorted names in IG), likely meaning the bonds overtightened. We therefore could see widening in the near term now that the technical drivers are gone. Also, the negative outlook by Moody's adds more risk to the credit. We therefore downgrade our recommendation on EQT to UW from MW.

EQT Corp (EQT) Key Data	2022A	2023A	2024E
Operating (US$ mm)			
Revenues	10,024	2,895	2,557
Adjusted EBITDA	3,526	2,983	1,811
Balance Sheet (US$ mm)			
Cash	1,459	81	5
Total Debt	5,679	5,795	6,748
Net Leverage (x)	1.2	1.9	3.7

Source: Company filings & BofA Global Research.

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Refer to important disclosures on page 6 to 9. Analyst Certification on page 5. Valuation & Risk on page 5. **12669663**

Timestamp: 12 March 2024 09:37AM EDT

EQT to buy EQM in an-all stock deal

On Monday, EQT announced plans to acquire EQM in an all-stock transaction. Each outstanding share of EQM common stock will be exchanged for 0.3504 shares of EQT common stock. The combined business is expected to have an enterprise value of over $35b and close in 4Q24 subject to a shareholder vote at both companies. The transaction is contingent on the FERC authorizing EQM's Mountain Valley Pipeline (MVP) project to commence service (excepted in 2Q24). Boards of both companies have unanimously approved the deal. EQT shareholders are expected to own ~74% of the combined company with EQM shareholders owning the balance.

De-leveraging

EQT identified a "low risk path" to >$5b of near-term debt repayment via $3.5b of asset sales and free cash flow. On its call, management noted that debt repayment will be focused at the front-end of its capital structure. The combined business provided a long-term gross debt target of $7.5b which it plans to reach 12-18 months post-close. Separately, management affirmed its commitment to IG credit ratings.

Long-term capital structure

Until de-leveraging is complete, EQT does not plan to collapse EQM's capital structure. Management noted that EQM note holders "do not have the right to look up to the EQT parent" and that EQT does not have any obligations to EQM's notes. Longer-term, management plans to refinance its capital structure and "term it out" with long-term fixed coupon bonds.

Asset sales

To complete its $3.5b asset sale goal, EQT plans to focus on selling regulated assets at EQM, which could include its Mountain Valley Pipeline project, as well as the EQT's ongoing sale process of certain non-operating assets. Bloomberg reported in December that EQT's non-operating assets could be worth over $3b. On its call, EQT stated that it has over 2x the number of sales candidates necessary to reach its divestiture target.

Pro-forma guidance

In FY25, EQT expects PF EBITDA of ~$5.5b and free cash flow of ~$2.5b, at recent strip pricing. Over the long-term, EQT guided FY29 EBITDA of >$6.5b and free cash flow of >$4b. The PF business will be underpinned by ~30% of cash flow coming from Midstream assets.

Rating agency commentary

EQT has fully vetted the PF balance sheet with all three rating agencies to ensure the continuance of an IG credit rating. The combined business will be evaluated on a hybrid upstream / midstream ratings structure which reflects the integrated business model and improved cash flow durability. Separately, on Monday evening, Moody's placed EQT on outlook negative while affirming its Baa3 rating. The outlook reflects the company's high PF net leverage and uncertainty around the timing and amount of proceeds from proposed asset sales given currently low / volatile natural gas prices. Moody's could downgrade EQT if retained cash flow (RCF) to debt falls below 30% or if leverage full cycle ratio (LFCR) falls below 1.5x. An upgrade is unlikely but could occur if EQT reached its long-term debt target and consistently generates LFCR more than 2.5x and RCF to debt of 60% in a $3/mcf natural gas environment.

Synergies

Synergies are expected to be $250mm annually, includes financial & corporate costs of ~$120mm, uptime & production optimization of ~$75mm, and capital & operating costs of ~$55mm. The business has also identified a pathway to an incremental $175mm of annual synergies (no timeline provided).

EQM overview

EQM provides EQT with ~1,220 of high-pressure gathering pipelines, ~940 miles of FERC-regulated interstate pipeline (4.4 bcf/d of capacity), and ~200 miles of mixed-use water pipelines with ~350 mbbl/d of above ground storage. In addition, EQM owns ~49% of the Mountain Valley Pipeline project, ~300-mile FERC-regulated pipeline connecting Appalachia basins to the Southeast US. The project, which has capacity of 2 bcf/d, is expected to be in service in 2Q24. Separately, earlier this year EQM announced that it was working with advisors over a possible sale.

Exhibit 1: EQT Corp (EQT) model and forecast ($mm)

Under a $2.40/mmbtu (FY24) & $3.45/mmbtu (FY25) price deck, we expect EQT's PF net leverage to rise to 3.7x by YE24 but then fall to 2.2x by YE25

	2020	2021	2022	2023	1Q24E	2Q24E	3Q24E	4Q24E	2024E	2025E
Income Statement										
Gross Revenue	2,659	6,840	12,141	5,052	1,261	894	1,193	1,589	4,936	7,830
Transportation and processing	1,711	1,942	2,117	2,157	515	614	622	629	2,380	1,746
Net Revenue	948	4,898	10,024	2,895	746	280	571	960	2,557	6,084
Operation & Maintenance	-	-	-	-	-	-	-	-	-	-
Production	155	225	301	255	108	111	112	109	439	349
Exploration	5	24	3	3	5	6	6	6	22	23
Impairment of long-lived assets	101	312	391	109	-	-	-	-	-	-
SG&A	175	196	253	236	72	77	78	80	308	210
DD&A	1,419	1,677	1,666	1,732	438	470	476	486	1,870	1,979
Operating Income	(908)	2,463	7,410	559	123	(384)	(102)	280	(83)	3,523
Interest and related charges, net	271	309	250	220	51	59	65	66	240	511
Capitalized Interest	17	18	28	41	8	8	8	8	32	32
Total Interest Expense	288	327	278	261	59	67	73	74	272	543
Gain (Loss) on derivatives not designated as hedges	400	(3,775)	(4,643)	1,839	-	-	-	-	-	-
Equity in Income of Affiliates/Minority interest	(314)	72	(5)	8	-	-	-	-	-	-
Other, Net	(173)	(40)	(178)	(100)	1	1	1	1	2	2
Income Before Taxes	(1,266)	(1,589)	2,335	2,085	73	(442)	(166)	215	(321)	3,014
Income taxes (benefit)	(299)	(434)	554	369	15	(93)	(35)	45	(67)	633
Tax rate (%)	24%	27%	24%	18%	21%	21%	21%	21%	21%	21%
Income before non-recurring Items	(967)	(1,155)	1,781	1,716	58	(349)	(131)	170	(253)	2,381
Discon Ops/Non-Recurring Items	-	(1)	(10)	1	-	-	-	-	-	-
Net Income	(967)	(1,156)	1,771	1,717	58	(349)	(131)	170	(253)	2,381
Avg. Shares Outstanding	261	323	406	413	481	481	481	481	481	647
Per Share Earnings	-$3.71	-$3.58	$4.36	$4.16	$0.12	-$0.73	-$0.27	$0.35	-$0.53	$3.68
Cash settlements received (paid) on derivatives not designated as hedges	897	(2,159)	(5,955)	578	-	-	-	-	-	-
EBITDAX	1,515	2,336	3,526	2,983	566	92	381	772	1,811	5,527
Consenus	1,496	2,365	3,570	2,973	1,033	642	715	947	3,304	4,774
LTM Int. Exp.	288	327	278	261	263	281	285	272	272	543
LTM EBITDAX	1,515	2,336	3,526	2,983	2,270	2,001	1,861	1,811	1,811	5,527
LTM CFFO	1,399	2,029	3,366	2,795	2,030	1,741	1,615	1,527	1,527	4,803
Credit Metrics (LTM)										
EBITDAX / Interest Expense	5.3x	7.1x	12.7x	11.4x	8.6x	7.1x	6.5x	6.7x	6.7x	10.2x
Total Debt / EBITDAX	3.3x	2.3x	1.6x	1.9x	2.6x	3.2x	3.6x	3.7x	3.7x	2.2x
Net Debt/EBITDAX	3.2x	2.3x	1.2x	1.9x	2.6x	3.2x	3.6x	3.7x	3.7x	2.2x
Debt/Proved Boe	$1.49	$1.32	$1.36	$1.26	$1.28	$1.41	$1.48	$1.47	$1.47	$2.69
Debt/Proved Developed Boe	$2.17	$1.91	$1.95	$1.78	$1.81	$1.99	$2.08	$2.07	$2.07	$3.79
Balance Sheet										
Cash & Equivalents	18	114	1,459	81	5	5	5	5	5	400
Total Debt	4,925	5,485	5,679	5,795	5,885	6,472	6,793	6,748	6,748	12,370
Minority Interest	7	16	41	8	-	-	-	-	-	-
Common Equity	9,255	9,955	11,172	14,773	14,755	14,330	14,123	14,213	14,213	21,883
Book Capitalization	14,188	15,456	16,892	20,576	20,640	20,802	20,916	20,961	20,961	34,253
Net Debt	4,907	5,371	4,220	5,714	5,880	6,467	6,788	6,743	6,743	11,970

Source: Company Filings, BofA Global Research

*We assume a January 1, 2025, closing date for the EQM acquisition

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Valuation & risk

EQT Corp (EQT)

EQT is an independent E&P company with an emphasis on Appalachian-area natural gas supply, transmission, and distribution.

Pro-forma for the acquisition of Equitrans Midstream, we think EQT should benefit from an increase size and scale, asset diversification, a lower cost structure, and a more stable earnings stream. We also think the business could operate with a lower breakeven and produce significantly higher free cash flow over time. Importantly, we think EQT's 12-18 months debt paydown plan is manageable if strip pricing holds, though we have concerns around the expected near-term spike in PF leverage if natural gas prices struggle to rebound off recent low prices. Nonetheless, management will need to execute its asset sales regardless of natural gas prices. Compared to peers, we think spreads are skewed wider from current levels given EQT's higher PF leverage, our outlook for softer gas prices in 1H24 and tight trading levels. We therefore provide an UW rec on the name.

Risks: EQM transaction not closing / being delayed, slower-/faster-than-expected buildout of northeastern natural gas pipelines, additional bondholder-friendly actions, volatility in oil, natural gas, and NGL prices, changes in its capex program that either stress or relieve cash flow estimates, and shareholder-friendly activities that strain cash flows such as share repurchases and dividend increases.

Analyst Certification

I, Daniel Lungo, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Security/Loan pricing

EQT Corp / EQT

Security	Amt	Maturity date	Ratings Moody's/S&P/Fitch	Price	Price date	Yield (%)	Spread (bps)
3.9, Senior, USD, 2027:B	1,250	01-OCT-2027	Baa3/BBB-/BBB-	95.21	11-Mar-2024	5.40	114
7, Senior, USD, 2030:B	750	01-FEB-2030	Baa3/BBB-/BBB-	106.84	11-Mar-2024	5.62	152
6.125, Senior, USD, 2025:B	1,000	01-FEB-2025	Baa3/BBB-/BBB-	100.25	11-Mar-2024	5.83	77
5, Senior, USD, 2029:B	350	15-JAN-2029	Baa3/BBB-/BBB-	98.35	11-Mar-2024	5.39	124
3.125, Senior, USD, 2026:B	500	15-MAY-2026	Baa3/BBB-/BBB-	94.86	11-Mar-2024	5.67	115
3.625, Senior, USD, 2031:B	500	15-MAY-2031	Baa3/BBB-/BBB-	88.68	11-Mar-2024	5.56	148
5.75, Senior, USD, 2034:B	750	01-Feb-2034	Baa3/BBB-/BBB-	100.02	11-Mar-2024	5.75	166

For pricing information refer to “Other Important Disclosures” below.
B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); CDS=Credit Default Swap; EP=Equity Preferred

Disclosures

Important Disclosures

Credit opinion history

EQT Corp / EQT

Company	Date[R1]	Action	Recommendation	
EQT Corp / EQT	28-Feb-2021		NA	
	25-Oct-2021	Coverage Reinstatement	Underweight	
	11-Jul-2022	Extended Review	NA	
	11-Jul-2022	Coverage Reinstatement	Overweight	
	08-Dec-2022	Downgrade	Marketweight	
Security	**Date[R1]**	**Action**	**Recommendation**	**Price**
3.9, Senior, USD, 2027:B	28-Feb-2023		Marketweight	
7, Senior, USD, 2030:B	28-Feb-2023		Marketweight	
6.125, Senior, USD, 2025:B	28-Feb-2023		Marketweight	
5, Senior, USD, 2029:B	28-Feb-2023		Marketweight	
3.125, Senior, USD, 2026:B	28-Feb-2023		Marketweight	
3.625, Senior, USD, 2031:B	28-Feb-2023		Marketweight	
5.75, Senior, USD, 2034:B	19-Jan-2024	New Issue	Marketweight	99.79

Table reflects credit opinion history as of previous business day’s close.[R1]First date of recommendation within the last 36 months, if for an issuer or within the last 12 months, if for a security or loan. The investment opinion system is contained at the end of the report under the heading "BofA Global Research Credit Opinion Key."
Pricing information in the table is provided for each action where available. In the case of bonds, loans, capital securities and equity preferreds, the price shown reflects the nominal cash price for the security; and in the case of CDS, the price shown reflects the spread, on the date of the relevant action.
B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); EP=Equity Preferred; CDS=Credit Default Swap

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Underweight: Spreads and/or excess returns are likely to underperform the relevant and comparable market over the next three months.

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Buy Protection: Buy CDS, therefore going short credit risk.
Neutral: No purchase or sale of CDS is recommended.
Sell Protection: Sell CDS, therefore going long credit risk.

Corporate Credit Issuer Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships R2	Count	Percent
Buy	144	37.21%	Buy	119	82.64%
Hold	193	49.87%	Hold	163	84.46%
Sell	50	12.92%	Sell	37	74.00%

R2 Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only corporate credit issuer recommendations. A corporate credit issuer rated Overweight is included as a Buy, a corporate credit issuer rated Marketweight is included as a Hold, and a corporate credit issuer rated Underweight is included as a Sell.

Credit Opinion History Tables for the securities referenced in this research report are available on the Price Charts and Credit Opinion History Tables website, or call 1-800-MERRILL to have them mailed.
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