Pembina (PBA): Initiate Position 1.25% **May 2022**

Company Overview

PBA owns an integrated system of pipelines that transport various hydrocarbon liquids and natural gas products produced primarily in Western Canada. The company also owns gas gathering and processing facilities; an oil and natural gas liquids infrastructure/logistics business; and is growing an export terminals business. PBA's integrated assets and commercial operations along much of the hydrocarbon value chain allow it to offer a full spectrum of midstream and marketing services to the energy sector.

Pembina is committed to identifying additional opportunities to connect hydrocarbon production to new demand locations through the development of infrastructure that would extend the company's service offering even further along the hydrocarbon value chain. PBA is structured into three divisions: Pipelines, Facilities and Marketing-New Ventures Division

Pipelines

PBA provides customers with pipeline transportation, storage, and rail services in key market hubs in Canada and the US for crude oil, condensate, natural gas liquids and natural gas. The division manages pipeline transportation capacity of 3.1million boe/d (barrels of oil equivalent per day), above ground storage of 11 million barrels and rail transportation capacity of approximately 145 thousand boe/d within its conventional, oilsands, and heavy oil and transmission assets.

The conventional assets gather and transport light and medium crudes, condensate, and natural gas liquids from Western Alberta and Northeast British Columbia to the Edmonton, Alberta area for either further processing or transportation on downstream pipelines. The oil sands and heavy oil assets transport heavy and synthetic oil produced within Alberta to the Edmonton area and offer associated storage, transportation, and rail services. The transmission assets transport natural gas, ethane, and condensate throughout Canada and the United States on long haul pipelines linking various key market hubs.

The Pipelines Division assets supply products from hydrocarbon producing regions to refineries, fractionators, and market hubs in Alberta, British Columbia, Illinois, and California, as well as other regions throughout North America.

Facilities Division

Pembina's natural gas gathering, and processing assets are strategically positioned in active, liquid rich areas of the Western Canada Sedimentary Basin (WCSB), Williston Basin and are integrated with the Company's other businesses. It includes approximately 354 thousand boe/d of NGL fractionation, 21 million barrels of cavern storage and associated pipeline and rail termination facilities, and PBA's recently completed construction of a liquified propane export facility on Canada's West Coast.

Pembina also owns a 125-acre bulk marine export terminal in Vancouver, British Columbia. The facility consists of four vessel berths with rail infrastructure serviced by three Class 1 railways that receive and unload unit trains, conveyance systems, and significant dry bulk and liquid storage capacity. It also is equipped with efficient material handling systems to load and unload ocean-going vessels.

Marketing and New Ventures

Within the Marketing & New Ventures Division, Pembina undertakes value-added commodity marketing activities, including buying and selling products (natural gas, ethane, propane, butane, condensate and crude oil), commodity arbitrage, and optimizing storage opportunities. The marketing business enters into contracts for capacity on both PBA's and third-party infrastructure, handles proprietary and customer volumes and aggregates production for onward sale.

Transitional Strategies

PBA is actively increasing the services that it can provide to its clients that will make it more than a traditional midstream company. The firm also is incorporating different partnerships in pursuit of these goals including partnering with Canadian indigenous tribes and private equity firm KKR.

- PBA is continuing to move up the natural gas value chain from pipelines to gathering and processing assets. A recent deal with KKR created "Newco", a joint venture with KKR that will be 60% owned and fully operated by PBA. This will significantly expand the company's exposure to processing and gathering assets in Western Canada. PBA has expressed some interest in eventually getting into Petrochemical production but does not participate in this segment of the hydrocarbon value chain at this time.
- PBA continues to be focused on creating capabilities to deliver Western Canadian energy products to Asia and South America using West Coast facilities, reducing transportation costs for its customers. The company does operate the Prince Rupert LPG (liquefied petroleum gas) export terminal on Watson Island, British Columbia. It is essentially a small-scale rail terminal where LPG can be moved from rail cars to smaller vessels for delivery to foreign markets. The company has the potential to expand this facility but has deferred the project at this time. PBA has partnered with the Haisla Nation, an indigenous tribe, to develop Cedar LNG (liquid natural gas), a proposed floating LNG facility in Kitimat, British Columbia, within the traditional territory of the Haisla nation. Cedar LNG Is strategically positioned to leverage Canada's abundant natural gas supply and BC's growing liquified gas (LNG) infrastructure. The final investment decision on the project is expected in the second half of 2023.
- PBA and its partner, TC Energy, are proposing the construction of the Alberta Carbon Grid (ACG). The ACG is a carbon transportation and sequestration system which, when fully constructed, would be capable of transporting more than 20 million tons of carbon dioxide annually. It is designed to be an open access system that will serve as the backbone of carbon capture, utilization, and storage (CCUS) in Alberta by connecting regions of large concentrations of emissions to key storage locations. PBA and TC Energy submitted an application to the Government of Alberta to build and operate ACG in the province's industrial heartland near Edmonton. During the first quarter the government of Alberta announced that ACG had been one of the projects chosen to move to the next stage of the province's carbon capture program.

Positives

- PBA is committed to build its business within its established Financial Guardrails. These provide a strong foundation for the dividend even as PBA incorporates some level of commodity risk. The guardrails are:
    - Maintain target of 80% fee-based contribution to adjusted EBITDA
    - Target <100% dividend payout of fee based distributable cash flow
    - Target 75% credit exposure from investment grade and secured counterparties
    - Maintain strong BBB credit rating (investment grade)

- The company operates in an energy rich geography with access to the Western Canada Sedimentary Basin in British Columbia and Alberta
- PBA has numerous investment opportunities to expand the scope and reach of its current pipeline and processing system.
- PBA has developed a partnership with KKR. The first transaction was the creation of a "Newco" with assets contributed by PBA and KKR that also will include the assets of Energy Transfer Canada. PBA will own 60% of the "Newco" and fully operate it. KKR owns the remaining 40%. KKR and PBA have agreed to pursue field-based natural gas gathering and processing assets in western Canada within "Newco". The transaction is expected to close in Q3 2022. PBA announced that its dividend will be increased by 3.6% when the transaction officially is closed.
- PBA is actively working with Canadian indigenous peoples on various projects. This is a positive for the tribes and adds to the viability and regulatory acceptance of new projects. For example, Chinook Pathways is an indigenous-led partnership formed to pursue equity ownership in the Trans Mountain Pipeline following the completion of the construction of the Trans Mountain Expansion. Chinook Pathways was formed by the Western Indigenous Pipeline Group (WIPG), a wholly-owned Indigenous company led by Chiefs and community leaders representing the indigenous communities directly in the path of Trans Mountain in B.C. and Alberta, and its selected industry partner, PBA. The goal is for WIPG to acquire a stake in Trans Mountain for the benefit of the Indigenous communities that live along the pipeline. This should alleviate the opposition of the indigenous people to the construction of the pipeline expansion, increasing the probability that this important project will be completed. PBA will play an important role in bringing this project to fruition.

<u>Negatives</u>

- Financial Guardrails could limit potential acquisitions (need to maintain fee-based to commodity ratio) as well as future dividend growth
- PBA is a Canadian company that introduces additional currency risk into the LCV portfolio
- Development of West coast export facilities has met heavy resistance from environmental groups and governmental entities. It may be difficult to realize the company's strategy to export energy products directly to Asia and South America.
- While the regulatory climate in Canada appears to be more amenable to the energy industry than the US, it could quickly change
- PBA's YTD stock performance has made valuations less attractive than earlier in the year. However, we believe that the number of potential projects in the hopper and the general fundamentals of the energy market still make this a good time to initiate a position.
- PBA's charismatic CEO, Mick Dilger, abruptly resigned in late November 2022 to pursue other opportunities. He was replaced by Scott Burrows who had served as Pembina's CFO for approximately seven years. While the company appears to be operating smoothly (the KKR deal occurred under CEO Burrows), it is always a little disconcerting when a CEO unexpectedly resigns.

Current & Historical Valuations

Valuation Matric	Current	5-Year High	5-Year Low	Average	Vs. Industry
Price to Earnings (PE)	23.7	42.8	5.3	22	1.2
Forward PE	17.2	23.5	6.2	17.5	1.0
Price to Expected Growth (PEG)	2.4	12.9	.7	2.7	.7
Price to Book Value	2.2	2.7	.5	1.9	1.2
Price to Cash Flow	10	17.5	2.9	11	.9
Enterprise Value to EBITDA	12.1	20.0	8.3	13.5	.8
Enterprise Value to Sales	4.1	5.7	2.6	4.2	.9
Dividend Yield	5.1	16.8	4.0	5.6	.9

Note:

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