SJW Group (SJW)

Updated April 13th, 2018 by Nate Parsh

Key Metrics

Current Price:	$53	**5 Year CAGR Estimate:**	9.7%	**Quality Percentile:**	N/A
Fair Value Price:	$53	**5 Year Growth Estimate:**	7.6%	**Momentum Percentile:**	N/A
% Fair Value:	100%	**5 Year Valuation Multiple Estimate:**	0.0%	**Total Return Percentile:**	N/A
Dividend Yield:	2.1%	**5 Year Price Target**	$77	**Valuation Percentile:**	N/A

Overview & Current Events

SJW Group is a water utility company that produces, purchases, stores, purifies and distributes water to consumers and businesses in the Silicon Valley area of California and the area north of San Antonio, Texas. The company also has a small real estate division that owns and develops properties for both residential and warehouse customers in California and Tennessee.

SJW announced adjusted earnings of $0.43 per share on 2/22/2018. This was $0.01 below estimates. Revenue grew 18% year-over-year to $93.5 million, $10.5 million above expectations. A 3.5% increase in water rates helped SJW's results.

On 3/14/2018 SJW announced that it will be merging with Connecticut Water Service (CTWS). This merger will add 135,000 customers in Connecticut and Maine to SJW's customer base. The addition of CTWS will transform SJW into the third largest water utility company. This merger will also diversify SJW's customer base.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.08	$0.81	$0.84	$1.11	$1.18	$1.12	$2.54	$1.85	$2.57	$2.45	***$2.66***	***$3.84***
DPS	$0.65	$0.66	$0.68	$0.69	$0.71	$0.73	$0.75	$0.78	$0.81	$1.04	***$1.12***	***$1.61***

SJW's earnings per share often vary wildly from year to year. The company saw earnings decline at the height of the last recession. Earnings-per-share (EPS) growth over the past 10 years is 8.5%. This is an impressive growth rate for a water utility company. CTWS has grown EPS at an average rate of 6.7% over the same time frame. Using the average growth rate of the two companies (7.6%) applied to 2018's estimated EPS of $2.66, the combined company could see $3.84 EPS by 2023.

SJW has increased its dividend for the past 51 years. The average dividend growth rate over the past ten years is 4%. CTWS, which has raised dividends for 48 years, has grown its dividend 3% per year over the same time period. We expect the combined company to maintain a payout ratio of around 42%, in line with SJW's recent history. This implies a dividend of $1.61/share by 2023.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	26.2	28.7	29.1	21.2	20.4	24.3	11.2	16.6	15.7	18.8	***19.9***	***20***
Avg. Yld.	2.3%	2.8%	2.8%	2.9%	3.0%	2.7%	2.6%	2.5%	2.0%	1.9%	***2.1%***	***1.6%***

Price to earnings multiples for water utilities tend to be high, but SJW's multiple was extremely high in the 2008-2010-time period. This could mean that investors were paying far too much for growth during this time. Investors shouldn't expect to see this type of multiple unless the company grows earnings at a higher than expected rate.

Investors hold shares of utility companies for their dividend yields, but SJW has only seen a yield above 3.0% once in the past 10 years (2012). Investors shouldn't expect SJW, or any other water utility stock, to offer a high yield. DPS has grown at half the rate that EPS has over the last decade. If the merger with CTWS leads to further earnings growth, then the possibility of higher dividend growth exists.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	15.3%	15.1%	13.7%	14.1%	14.2%	14.1%	15.5%	14.5%	14.9%	15.9%	***16.4%***	***15%***
Debt/A	70.1%	71.2%	72.7%	74.6%	74.7%	71.1%	71.6%	71.3%	70.8%	68.2%	***71.6%***	***70.6%***
Int. Cov.	2.5	1.8	3.6	2.8	2.9	2.8	4.7	3.8	5	5.2	***4.4***	***3.5***
Payout	60.2%	81.5%	81%	62.3%	60.2%	65.2%	29.5%	42.2%	31.5%	42.4%	***42.1%***	***42.0%***
Std. Dev.	62.1%	43.1%	33.1%	32.7%	21.6%	23.6%	23.5%	26.6%	31.5%	26.3%	***27.5%***	***32.4%***

Many investors own utility companies for their reliable earnings and dividends, especially for uncertain economic times. During the last recession, SJW experienced a decline in earnings that took several years to recover. Dividend growth declined during this time, but the stock's yield reached as high as 3%.

A major competitive advantage for SJW is that it operates in two areas, Silicon Valley and Central Texas, that have seen high levels of population growth in recent years. These areas need improved water infrastructure to serve a growing client base, so local governments often allow the company to raise rates at a relatively high level in order to fund these projects. For example, SJW is approved for a 4.2% increase in 2018 for its customers in the Silicon Valley area. The company applied for rate increases of 9.8%, 3.7% and 5.2% over the next three years for this area.

Dividend growth over the past decade is less than half of SJW's earnings growth. Because of this, SJW has a low payout ratio for a utility. The company's dividend growth is rather conservative, but this allows SJW to have its dividend remain intact and growing if the company's earnings were to decline.

An additional issue that investors should be aware of is that SJW's earnings are highly concentrated in California (60% of expected sales post CTWS merger) and Connecticut (30% of expected sales post CTWS merger).

Final Thoughts & Recommendation

Shareholders of SJW could be in line to see a total return of between 9% and 10% per year through 2023. This total return is arrived at by a combination of growth (~7.5%), dividends (~2%) and multiple growth (~0%). This high level of growth per year could be attractive to growth investors. Investors with a defensive mindset or those looking to diversify the utility portion of their portfolio could be rewarded for adding SJW to their holdings.

Total Return Breakdown by Year