



Fortis, Inc. (FTS)

Updated November 9th, 2018 by Josh Arnold

Key Metrics

Current Price:	\$45	5 Year CAGR Estimate:	12.1%	Volatility Percentile:	1.3%
Fair Value Price:	\$50	5 Year Growth Estimate:	6.0%	Momentum Percentile:	37.2%
% Fair Value:	90%	5 Year Valuation Multiple Estimate:	2.1%	Growth Percentile:	48.1%
Dividend Yield:	4.0%	5 Year Price Target	\$67	Valuation Percentile:	71.3%
Dividend Risk Score:	B	Retirement Suitability Score:	A	Total Return Percentile:	75.1%

Overview & Current Events

Fortis is Canada's largest investor-owned utility business with operations in Canada, the United States, and the Caribbean. It is cross-listed in Toronto and New York, where it trades with a market capitalization of CAD\$19.2 billion. Fortis has increased its dividend for 45 consecutive years and trades with a current after-tax yield of 3.4% (4.0% before the 15% withholding tax applied by the Canadian government). Canadian Dollars are used in this research report.

Fortis reported Q3 earnings on 11/2/18 and results were largely in line with expectations. Total revenue was up 7.3% as the company benefited from a variety of factors. Favorable foreign exchange rates contributed, as did higher electricity sales and rate base growth. Margins fell, however, as net income came in flat against the year-ago quarter on a dollar basis. Culprits included higher energy supply costs, particularly at subsidiary UNS Energy, as it saw higher commodity costs and negative impacts from seasonality. Operating expenses rose year-over-year, but it was due almost entirely to a one-time break fee the company received in last year's Q3; on a comparable basis, operating expenses were mostly flat. In total, earnings-per-share came in at 65 cents against 61 cents in the year-ago quarter and kept Fortis on track to hit our earnings-per-share estimate of \$2.60 for this year.

Fortis continues to reiterate its growth target of 6% annually and we've used that number to compute our earnings estimates in the out years. Fortis also noted it was well on its way to completing its planned \$3.2 billion in capital spending for this year, in addition to noting it was lifting its capital spending to \$3.5 billion annually for the next five years. This spending is critical for supporting growth. The hike in capex should be a net positive for shareholders..

The company also recently boosted its dividend to 45 cents per quarter and said it expected rate base growth of 7.1% annually for the next three years and 6.3% annually for the next five years, respectively. Fortis' slate of planned and in-progress projects is impressive, and we believe it will have little trouble hitting its targets.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS¹	\$1.52	\$1.51	\$1.62	\$1.74	\$1.65	\$1.63	\$1.38	\$2.11	\$1.89	\$2.66	\$2.60	\$3.48
DPS¹	\$1.00	\$1.04	\$1.12	\$1.17	\$1.21	\$1.25	\$1.30	\$1.43	\$1.55	\$1.65	\$1.80	\$2.50
Shares	157	170	173	182	190	203	226	279	309	416	430	640

Fortis has compounded its earnings-per-share at 6.4% per year since 2008, and we expect 6% annually moving forward, per management's guidance and despite an ever-rising share count. Our estimates call for 9% annual growth in Fortis' share count, which is actually lower than the company's historical growth rate, which is closer to 12% annually.

Fortis' future growth will be driven by a substantial capital expenditure plan that the company is currently executing, as mentioned above. The capital expenditure plan is focused on areas like grid improvement, natural gas distribution, cyber protection, and clean energy. Importantly, this growth rate is *before* the impact of acquisitions, which have historically been important for Fortis. We see growth in the dividend roughly keeping pace with earnings growth and the share price, so the yield should remain near 4% for the foreseeable future (before mandatory withholding).

¹ All figures in Canadian dollars.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Fortis, Inc. (FTS)

Updated November 9th, 2018 by Josh Arnold

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	17.5	16.4	18.2	18.8	20.1	20.0	24.3	18.0	21.6	16.8	17.3	19.2
Avg. Yld.	3.8%	4.2%	3.8%	3.6%	3.6%	3.8%	3.9%	3.8%	3.8%	3.7%	4.0%	3.7%

Using our 2018 earnings-per-share estimate of \$2.60, Fortis is currently trading at a price-to-earnings ratio of 17.3, which we believe is well below fair value at 19.2. That implies a 2.1% tailwind to total returns from a rising valuation.

Fortis is currently trading with a dividend yield of 4.0% (gross of the withholding tax paid to the Canadian government), providing investors with a compelling opportunity to generate meaningful portfolio income in the international markets.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	16.0%	15.2%	15.3%	14.4%	14.3%	13.6%	12.2%	14.5%	9.4%	12.4%	13.0%	13.0%
Debt/A	68.3%	69.8%	68.6%	65.2%	63.8%	64.4%	65.3%	64.1%	65.7%	65.0%	65.0%	65.0%
Int. Cov.	1.9	1.9	2.1	2.3	2.2	2.2	1.9	3.0	2.3	2.9	2.5	2.5
Payout	65.8%	68.9%	69.1%	67.2%	73.3%	76.7%	94.2%	67.8%	82.0%	62.0%	66.1%	66.7%
Std. Dev.	22.9%	14.8%	14.6%	12.3%	8.0%	10.6%	10.5%	15.1%	13.7%	9.4%	13.0%	13.0%

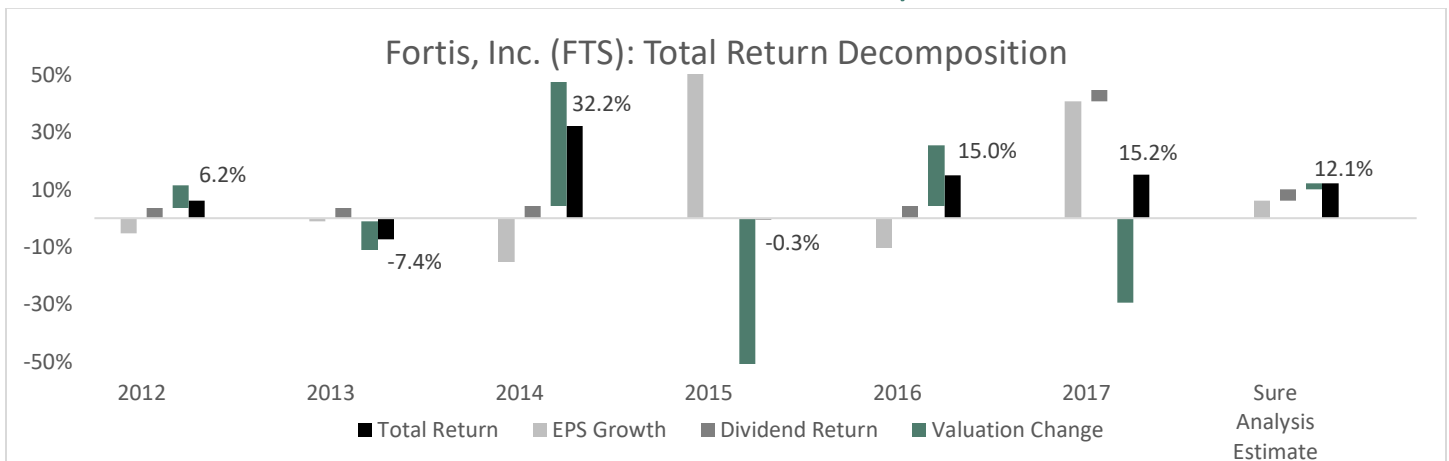
Fortis' gross profits have declined over time while its leverage ratios and interest coverage have improved. More importantly, what stands out is the stock's remarkably low stock price volatility. The company has posted single-digit price standard deviation in 2 of the last 10 years. Accordingly, Fortis appeals for investors who recognize that they may have trouble stomaching prolonged levels of heightened volatility in their investment portfolios.

Qualitatively, Fortis' competitive advantage is its size and scale in the fragmented Canadian utility industry. In addition, Fortis is unique because of its cross-border exposure. Three multi-billion acquisitions in the last five years have caused Fortis to now generate more than half of its revenue from the United States.

Final Thoughts & Recommendation

Even under conservative assumptions, Fortis appears positioned to deliver 12.1% total returns over long holding periods. Moreover, the company is likely to do so with far less volatility than the stock market averages. Accordingly, we are recommending Fortis as a buy for conservative, income-oriented investors who are averse to portfolio volatility.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Fortis, Inc. (FTS)

Updated November 9th, 2018 by Josh Arnold

Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	3903	3643	3657	3738	3654	4047	5401	6757	6838	8301
Gross Profit	1791	1844	1971	2041	2132	2430	3204	4166	4497	5940
Gross Margin	45.9%	50.6%	53.9%	54.6%	58.3%	60.0%	59.3%	61.7%	65.8%	71.6%
D&A Exp.	345	360	408	416	470	541	688	873	983	1179
Operating Profit	700	701	739	775	794	852	1023	1419	1483	2500
Operating Margin	17.9%	19.2%	20.2%	20.7%	21.7%	21.1%	18.9%	21.0%	21.7%	30.1%
Net Profit	259	280	313	357	362	410	379	805	660	1028
Net Margin	6.6%	7.7%	8.6%	9.6%	9.9%	10.1%	7.0%	11.9%	9.7%	12.4%
Free Cash Flow	-274	-343	-341	-256	-154	-276	-743	-570	-177	-268
Income Tax	65	49	67	84	61	32	66	223	145	588

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	11166	12139	12909	14214	14950	17908	26233	28804	47904	47822
Cash & Equivalents	66	85	109	87	154	72	230	242	269	327
Acc. Receivable	681	595	655	588	525	333	448	451	474	461
Inventories	229	178	168	134	133	143	321	337	372	367
Goodwill & Int.	1848	1846	1877	1890	1893	2420	4193	4714	13375	12725
Total Liabilities	7628	8476	8850	9271	9540	11532	17121	18451	31454	31073
Accounts Payable	874	852	953	457	498	423	612	414	554	696
Long-Term Debt	5294	5691	5967	5992	6083	7414	10819	11735	22282	21668
Total Equity	3046	3193	3305	3823	3992	4772	6871	8060	12974	13380
D/E Ratio	1.56	1.61	1.53	1.27	1.19	1.24	1.24	1.19	1.53	1.44

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	2.4%	2.4%	2.5%	2.6%	2.5%	2.5%	1.7%	2.9%	1.7%	2.1%
Return on Equity	9.2%	9.0%	9.6%	10.0%	9.3%	9.4%	6.5%	10.8%	6.3%	7.8%
ROIC	3.0%	3.1%	3.2%	3.4%	3.2%	3.2%	2.2%	3.8%	2.2%	2.7%
Shares Out.	157	170	173	182	190	203	226	279	309	416
Revenue/Share	22.47	19.71	19.55	19.67	18.53	19.34	23.89	23.73	21.82	19.94
FCF/Share	-1.58	-1.86	-1.82	-1.35	-0.78	-1.32	-3.29	-2.00	-0.56	-0.64

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.