



American States Water Co. (AWR)

Updated March 23rd, 2020 by Samuel Smith

Key Metrics

Current Price:	\$86	5 Year CAGR Estimate:	-3.4%	Market Cap:	\$3.2B
Fair Value Price:	\$57	5 Year Growth Estimate:	2.7%	Ex-Dividend Date:	5/13/20 ¹
% Fair Value:	151%	5 Year Valuation Multiple Estimate:	-7.9%	Dividend Payment Date:	6/2/20 ²
Dividend Yield:	1.5%	5 Year Price Target	\$65	Years Of Dividend Growth:	19
Dividend Risk Score:	A	Retirement Suitability Score:	C	Last Dividend Increase:	10.9%

Overview & Current Events

American States Water is a utility company with two business units: Utilities (primarily water, some electricity) and Services (wastewater services on several US military bases). American States Water is based in California, where it operates its utilities business. The company's services unit spans several US states. American States Water is a Dividend King, which means it has 50+ years of rising dividends. The company has a small market capitalization of just \$3.2 billion. American States Water reported its fourth quarter earnings results on February 24th. Diluted earnings-per-share surged by 22% year-over-year during the quarter and full-year adjusted earnings-per-share increased by a whopping 30%, driven by growth across all business segments. The company also benefited from a CPUC electric general rate case decision in August that was retroactive back to January 1, 2018, resulting in significant accretion to company earnings.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$1.11	\$1.12	\$1.41	\$1.61	\$1.57	\$1.60	\$1.62	\$1.67	\$1.72	\$2.24	\$2.28	\$2.60
DPS	\$0.52	\$0.55	\$0.64	\$0.76	\$0.83	\$0.87	\$0.91	\$0.99	\$1.06	\$1.22	\$1.26	\$1.58
Shares³	37	38	39	39	38	37	37	37	37	37	37	36

American States Water operates in a low-growth industry, therefore its earnings-per-share growth rate is not very high. Between 2009 and 2018 American States Water was able to grow its earnings-per-share at a rate of 8.7% annually, but more recently its growth rate has slowed down considerably. On the other hand, the company managed to increase its profitability even during the last financial crisis, which shows that American States Water's profitability is not cyclical. We do not expect it to suffer from the current coronavirus outbreak or any related economic fallout as it provides essential services to consumers regardless of the state of the economy.

American States Water's utility business will most likely continue to grow at a slow pace, as regulators will allow the company to increase its rates over time in order to encourage spending on growth and maintenance projects. The company is building out its services business by getting contracts for wastewater services on additional US military bases. The contracts for wastewater services on US military bases span a 50-year period each, so getting one such contract provides for a decades-long and very safe revenue stream. Receiving one new contract every couple of years provides for solid revenue growth potential. On a quarterly basis, revenues can still see ups and downs depending on the amount of construction activity on military bases. American States Water should be able to increase its profits going forward. A mid-single-digits earnings-per-share growth rate seems highly achievable, based on the further expansion of American States Water's services business and some profit increases for the utilities business.

American States Water has increased its dividend every year for more than fifty years in a row, which can only be described as a very long and successful dividend growth track record. The dividend growth rate was 6.9% during the last five years, which was possible due to an increase in its payout ratio.

¹ Estimate

² Estimate

³ In millions

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.



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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	15.7	15.4	14.3	17.2	20.1	24.6	25.6	27.5	38.2	42.0	37.7	25.0
Avg. Yld.	3.0%	3.2%	3.1%	2.7%	2.6%	2.2%	2.2%	2.0%	1.7%	1.4%	1.5%	2.4%

American States Water performed relatively well during the last financial crisis, which explains why the company's stock continued to trade at a valuation that is elevated. Its valuation has expanded further since as the stock's run-up over the last year has led to a very high price to earnings multiple. We believe that the current valuation is unjustifiable, and we forecast meaningful headwinds to the stock's total returns from multiple compression, though increasingly low interest rates have prompted us to increase the fair value estimate to 25 times earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	63.0%	46.8%	49.1%	45.4%	47.2%	52.9%	54.4%	56.2%	59.3%	61.3%	55.2%	60.8%

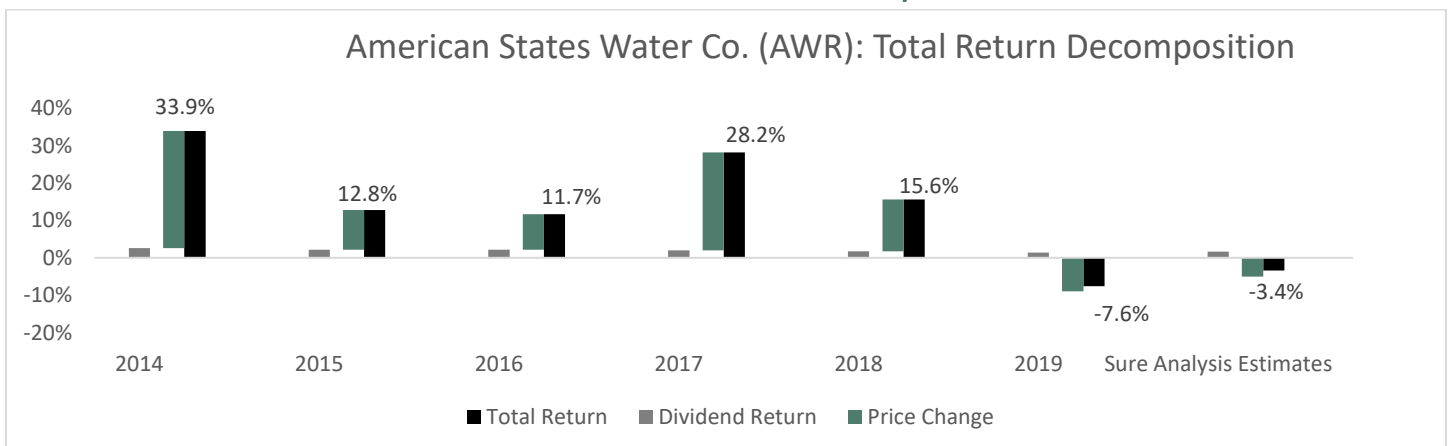
American States Water paid out roughly half of its net profits a year during the last decade. This is not a high payout ratio, especially for a stable company such as American States Water that generated strong earnings during the last financial crisis. We believe that the recession resilience, the moderate payout ratio, and the strong dividend growth track record mean that American States Water's dividend is very safe.

Utilities are not cyclical, and due to the decades-long contract durations with the US military, the services business is not cyclical either. American States Water is therefore quite recession-proof. There is a low risk of an earnings decline, shown by the fact that even during the last financial crisis, profits kept increasing. Competition is not a major issue for American States Water's business, as the company operates with very long-term contracts.

Final Thoughts & Recommendation

American States Water was a stable performer during the last financial crisis, and the company's dividend looks very safe for the foreseeable future. The company should be able to grow its profits during the coming years as well. American States Water nevertheless does not look like an attractive investment today, though, as its valuation is very high, which will pressure total returns significantly, as the meager 1.5% dividend yield and low-single-digits growth rate will be offset by significant valuation compression, leading to expected annualized total returns of -3.4%. As a result, we rate the stock a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	400	420	467	472	466	459	436	441	437	474
Gross Profit	280	301	350	357	349	338	333	337	328	354
Gross Margin	70.2%	71.6%	75.0%	75.6%	74.9%	73.7%	76.4%	76.5%	75.1%	74.6%
SG&A Exp.	86	74	71	77	78	80	82	82	83	83
D&A Exp.	40	41	43	41	42	43	39	39	41	36
Operating Profit	73	95	111	119	119	118	114	119	101	127
Operating Margin	18.3%	22.6%	23.8%	25.2%	25.6%	25.8%	26.2%	27.0%	23.1%	26.8%
Net Profit	33	46	54	63	61	60	60	69	64	84
Net Margin	8.3%	10.9%	11.6%	13.3%	13.1%	13.2%	13.7%	15.7%	14.6%	17.8%
Free Cash Flow	-25	0	33	38	91	8	-33	31	10	(35)
Income Tax	23	30	36	36	38	38	35	39	18	25

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	1192	1238	1281	1310	1378	1344	1470	1417	1501	1,641
Cash & Equivalents	4	1	23	38	76	4	0	0	7	1
Accounts Receivable	25	19	19	24	19	19	20	26	23	21
Inventories	2	3	5	5	4	5	4	5	6	6
Goodwill & Int. Ass.	1	1	1	1	1	1	1	1	1	1
Total Liabilities	814	830	826	818	871	878	976	887	943	1,040
Accounts Payable	36	38	41	50	42	51	44	51	60	56
Long-Term Debt	361	343	336	332	326	349	411	380	417	486
Shareholder's Equity	378	409	455	492	507	466	494	530	558	602
D/E Ratio	0.96	0.84	0.74	0.68	0.64	0.75	0.83	0.72	0.75	0.81

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.9%	3.8%	4.3%	4.8%	4.5%	4.4%	4.2%	4.8%	4.4%	5.4%
Return on Equity	9.0%	11.7%	12.5%	13.2%	12.2%	12.4%	12.4%	13.5%	11.7%	14.5%
ROIC	4.7%	6.2%	7.0%	7.8%	7.4%	7.3%	6.9%	7.6%	6.8%	8.2%
Shares Out.	37	38	39	39	38	37	37	37	37	37
Revenue/Share	10.67	11.15	12.20	12.15	11.98	12.19	11.87	11.96	11.83	12.82
FCF/Share	-0.67	0.00	0.87	0.99	2.33	0.21	-0.90	0.85	0.28	(0.95)

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

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