Otter Tail Corporation (OTTR)

Updated March 31st, 2020 by Samuel Smith

Key Metrics

Current Price:	$44	**5 Year CAGR Estimate:**	7.7%	**Market Cap:**	$1.5B
Fair Value Price:	$44	**5 Year Growth Estimate:**	4.6%	**Ex-Dividend Date[1]:**	5/13/20
% Fair Value:	99%	**5 Year Valuation Multiple Estimate:**	0.2%	**Dividend Payment Date[2]:**	6/10/20
Dividend Yield:	3.3%	**5 Year Price Target**	$56	**Years Of Dividend Growth:**	7
Dividend Risk Score:	D	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	5.7%

Overview & Current Events

Otter Tail Corporation goes back to 1907 with its electric utility, which was founded in Fergus Falls, MN. The company eventually expanded into metal fabrication and plastics manufacturing and today, it has about $950 million in annual revenue split between utility, manufacturing and plastics operations. Otter Tail has a $1.5 billion market capitalization.

Otter Tail reported fiscal 2019 earnings on 2/17/20. Consolidated operating revenues increased by $3.1 million year-over-year to $919.5 million and consolidated net income grew by a strong 5.5% to $86.8 million. Diluted earnings-per-share and dividends-per-share grew by 5.3% and 5.7% year-over-year respectively.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$0.38	$0.45	$1.05	$1.37	$1.55	$1.56	$1.60	$1.86	$2.06	$2.15	***$2.22***	***$2.78***
DPS	$1.19	$1.19	$1.19	$1.19	$1.21	$1.23	$1.25	$1.28	$1.34	$1.40	***$1.44***	***$1.80***
Shares[3]	36	36	36	36	37	38	39	40	40	40	***40***	***42***

Otter Tail's earnings-per-share history has been fairly strong in the last decade, as earnings bottomed in 2010 and have grown every year since. Guidance for this year is for ~$2.22 and we see average growth of 5.3% going forward. Otter Tail will achieve this growth via revenue increases from its utility business – which is looking stronger now that North Dakota and South Dakota have approved rate increases – as well as continued strong performances in its other two, non-utility lines of business. It continues to increase margins as well and the diversification it offers over other utilities is certainly a strength that is showing its value. The company's manufacturing and plastics businesses have benefited from higher order rates as well as a lower income tax rate, while seeing gross margins tick higher over time. The higher operating expenses seen in prior quarters are uncharacteristic for Otter Tail, so we don't see any long-term impairment just yet. We see all of these factors as continuing until further notice and as a result, earnings should grow steadily in the coming years. Otter Tail's full rate case in South Dakota is still pending, but the company has a favorable relationship with its regulators, so we are optimistic that Otter Tail will continue to receive the rate increases it needs to grow revenue.

The dividend was stagnant from 2008 to 2013, as Otter Tail was not able to cover the payout with earnings. However, that situation has rectified itself as the company has managed to produce some robust earnings growth and as a result, the dividend is being raised again. This is an important factor for the stock and we see modest payout growth ahead.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	55.1	47.5	21.7	21.1	18.8	18.2	20.2	22.1	22.2	24.2	***19.8***	***20.0***
Avg. Yld.	5.7%	5.6%	5.2%	4.1%	4.1%	4.3%	3.9%	3.1%	2.9%	2.7%	***3.3%***	***3.2%***

[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.

Otter Tail Corporation (OTTR)

Updated March 31st, 2020 by Samuel Smith

The stock's price-to-earnings multiple has moved significantly lower in recent years after being artificially inflated due to low earnings-per-share from 2008 to 2011. However, today's multiple of 19.8 near its recent historical norm of 20 and as such, we see the stock as fairly valued. We think shares will remain around a multiple of 20 over time, causing a very modest tailwind to total returns moving forward. The yield should remain near where it is today at just above 3% as dividend increases keep pace with earnings-per-share growth, and Otter Tail remains a decent income stock choice among utilities.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	113%	87%	78%	79%	78%	69%	65%	65%	***65%***	***65%***

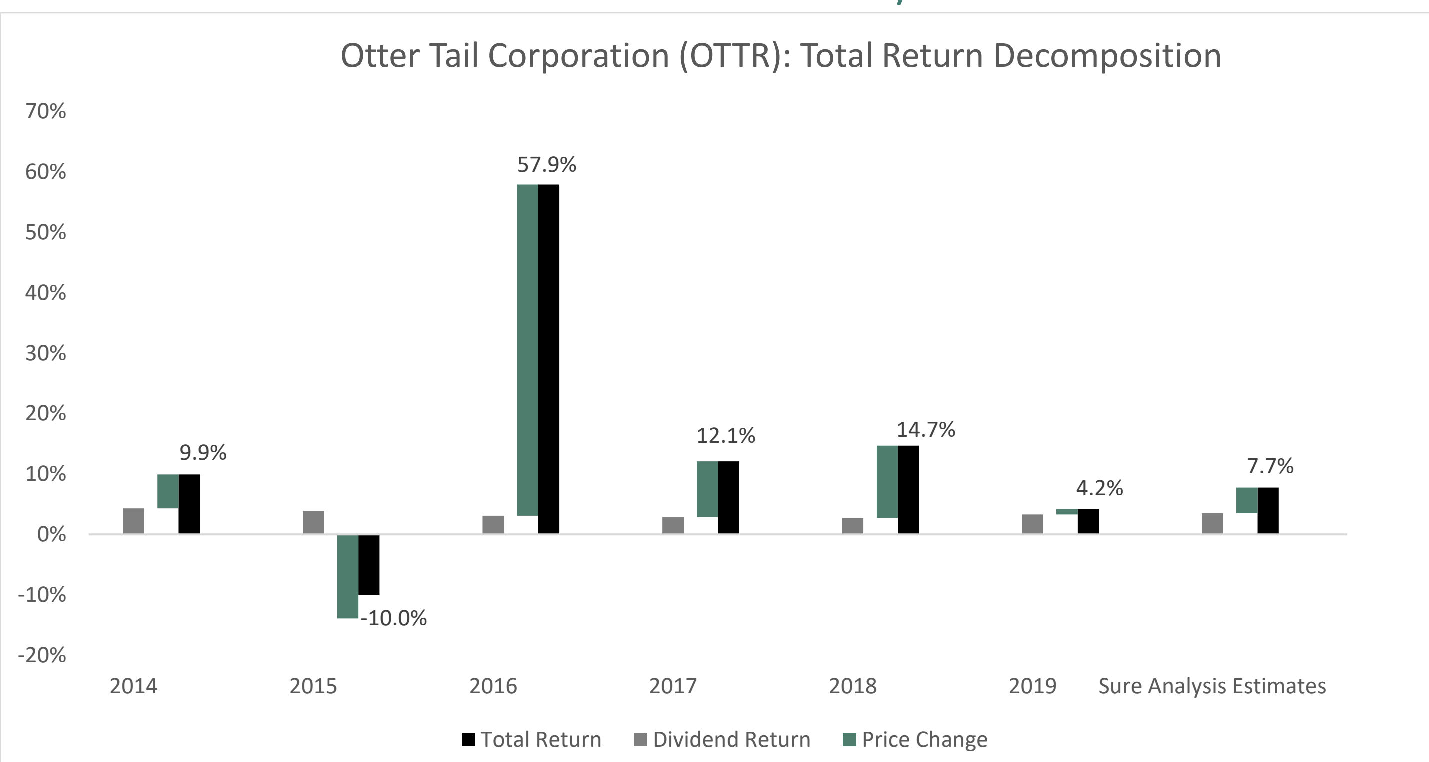
Otter Tail's payout ratio remains around two-thirds of earnings and we don't expect that will change. The company continues to boost its payout at roughly the same rate as earnings, so the dividend is quite safe and should continue to move higher over time.

Otter Tail's competitive advantage of having a diversified business model is also its disadvantage during recessions. The non-utility businesses are providing strong growth today but during the last recession, earnings fell much more than expected for a pure utility. That will likely happen next time there is a downturn, so investors should keep this in mind.

Final Thoughts & Recommendation

We see Otter Tail as a stock that has a relatively strong growth outlook compared to its peers and is trading right around fair value. We see the stock providing 7.7% annualized total returns moving forward along with a safe 3.3% dividend yield that will grow with inflation over time. As a result, it is a solid holding for conservative dividend growth investors, and we rate it a hold.

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.

Otter Tail Corporation (OTTR)

Updated March 31st, 2020 by Samuel Smith

Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	718	840	710	743	799	780	804	849	916	920
Gross Profit	169	180	193	192	204	210	229	246	256	264
Gross Margin	23.5%	21.4%	27.2%	25.9%	25.5%	26.9%	28.5%	29.0%	27.9%	28.7%
D&A Exp.	58	58	58	58	58	60	73	73	75	78
Operating Profit	65	72	95	94	100	109	117	132	129	135
Operating Margin	9.0%	8.6%	13.3%	12.7%	12.5%	14.0%	14.5%	15.6%	14.1%	14.7%
Net Profit	(1)	(13)	(5)	51	58	59	62	72	82	87
Net Margin	-0.2%	-1.6%	-0.7%	6.8%	7.2%	7.6%	7.8%	8.5%	9.0%	9.4%
Free Cash Flow	47	37	119	(12)	(51)	(43)	2	41	38	(22)
Income Tax	3	4	7	13	17	22	20	27	15	17

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	1,771	1,701	1,602	1,596	1,741	1,819	1,912	2,004	2,053	2,274
Cash & Equivalents	-	16	52	2	-	-	-	16	1	21
Accounts Receivable	95	93	91	58	60	63	68	68	75	78
Inventories	72	69	69	73	85	85	84	88	106	98
Goodwill & Int. Ass.	56	54	53	44	43	55	53	51	50	49
Total Liabilities	1,123	1,114	1,065	1,061	1,168	1,214	1,242	1,307	1,324	1,492
Accounts Payable	103	80	88	96	107	89	89	85	96	121
Long-Term Debt	513	472	422	441	510	577	581	603	609	696
Shareholder's Equity	632	571	522	535	573	605	670	697	729	781
D/E Ratio	0.79	0.80	0.78	0.82	0.89	0.95	0.87	0.87	0.84	0.89

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	-0.1%	-0.8%	-0.3%	3.2%	3.5%	3.3%	3.3%	3.7%	4.1%	4.0%
Return on Equity	-0.2%	-2.2%	-1.0%	9.6%	10.4%	10.1%	9.8%	10.6%	11.6%	11.5%
ROIC	-0.1%	-1.2%	-0.5%	5.3%	5.6%	5.2%	5.1%	5.7%	6.2%	6.2%
Shares Out.	36	36	36	36	37	38	39	40	40	40
Revenue/Share	19.93	23.29	19.60	20.45	21.75	20.70	20.75	21.37	22.97	23.01
FCF/Share	1.30	1.03	3.29	(0.33)	(1.39)	(1.13)	0.05	1.02	0.95	(0.56)

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