

Algonquin Power & Utilities Corp. (AQN)

Updated November 13th, 2020 by Kay Ng

Key Metrics

Current Price:	\$16	5 Year CAGR Estimate:	4.9%	Market Cap:	\$9.5B
Fair Value Price:	\$12	5 Year Growth Estimate:	6.5%	Ex-Dividend Date¹:	12/30/20
% Fair Value:	132%	5 Year Valuation Multiple Estimate:	-5.4%	Dividend Payment Date¹:	01/15/20
Dividend Yield:	3.9%	5 Year Price Target	\$17	Years Of Dividend Growth¹:	9
Dividend Risk Score:	F	Retirement Suitability Score:	D	Last Dividend Increase:	10%

Overview & Current Events

Algonquin Power & Utilities Corp. trades on both the Toronto Stock Exchange and New York Stock Exchange under the ticker, AQN. The renewable power and utility company was founded in 1988. All the figures in this report are in U.S. dollars unless otherwise noted.

The company has increased its dividend every year since 2011. The three parts of its business are regulated utilities (natural gas, electric, and water), non-regulated renewables (wind, solar, hydro, and thermal), and global infrastructure. Algonquin serves more than 1 million connections primarily in the U.S. and Canada. It also has renewable and clean energy facilities that are largely (about 93%) under long-term contracts with inflation escalations.

Algonquin reported its Q3 2020 results on 11/12/20. Revenue rose 3% against Q3 2019 to \$376 million. Adjusted net earnings rose 27%. Earnings-per-share (“EPS”) climbed 7%. Adjusted EBITDA was up 6%, while adjusted funds from operations rose 23%.

Year-to-date results indicate a resilient business through the pandemic. Revenue, adjusted EPS, and adjusted operating cash flow were essentially flat at \$1,185 million, US\$421 million and \$0.43, respectively. Adjusted EBITDA climbed 1% to \$616 million. Management’s 2020 EPS estimate remains at \$0.65-\$0.70. We continue to use the midpoint of roughly \$0.67 for our 2020 EPS estimate.

In October and November, Algonquin acquired ESSAL for \$162 million and Ascendant. ESSAL is a Chilean water utility that added ~230,000 connections. Ascendant’s major subsidiary is BELCO, the only electric utility in Bermuda. BELCO is a regulated utility and added ~36,000 connections. In August and November, Algonquin completed a solar and wind project in the U.S., adding a total of 245 MW capacity to its renewable energy portfolio.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$0.21	\$0.23	\$0.14	\$0.26	\$0.37	\$0.46	\$0.42	\$0.57	\$0.66	\$0.63	\$0.67	\$0.92
DPS	\$0.24	\$0.27	\$0.29	\$0.33	\$0.37	\$0.49	\$0.55	\$0.60	\$0.51	\$0.55	\$0.62	\$0.83
Shares¹	95	136	189	207	238	256	274	432	489	526	552	705

Investors should note that Algonquin previously paid Canadian dollar-denominated dividends and started paying a U.S. dollar-denominated dividend in 2014. It also began reporting in U.S. dollars in 2018. So, in the table above, the EPS from 2010 to 2017 are in Canadian dollars. To match the dividends with the earnings, the dividend-per-share is also displayed in Canadian dollars from 2010 to 2017. From 2018 and onwards, the data is in U.S. dollars. Historically, Algonquin’s EPS has been volatile. However, they have become more stabilized in the past few years, as the company has increased its scale with a more diversified asset base that is largely regulated utilities with predictable returns or renewable facilities with long-term contracts that generate stable cash flow. Specifically, its 2014 to 2019 EPS growth rate was 14.5% based on USD. It’s common for Algonquin to use equity as a source of capital to make acquisitions – its share count is more than five times it was from about 10 years ago. Going forward, it’s likely to issue new shares for growth. The company’s

1. Estimated dividend dates; Years of dividend growth based on reported currency of the company; Shares in millions.

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capital program through 2024 consists of \$9.2 billion of investments across its businesses, including more than \$6.7 billion in regulated opportunities. We forecast a slower EPS growth rate of 6.5% through 2025.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	21.7	24.9	47.4	27.3	22.9	22.4	27.5	22.3	15.7	19.0	23.7	18.0
Avg. Yld.	5.3%	4.7%	4.4%	4.6%	4.4%	4.8%	4.8%	4.7%	4.9%	4.6%	3.9%	5.0%

Taking out the outlier in 2012, from 2010 to 2019, the average price-to-earnings ratio was 22.6 and the average yield was 4.7%. Algonquin is a very different and much larger company versus a decade ago. We think a reasonable price-to-earnings of 18 makes sense for an anticipated slower (but still quite good) growth rate of 6.5%. We don't think Algonquin's yield would stray far away from 5%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

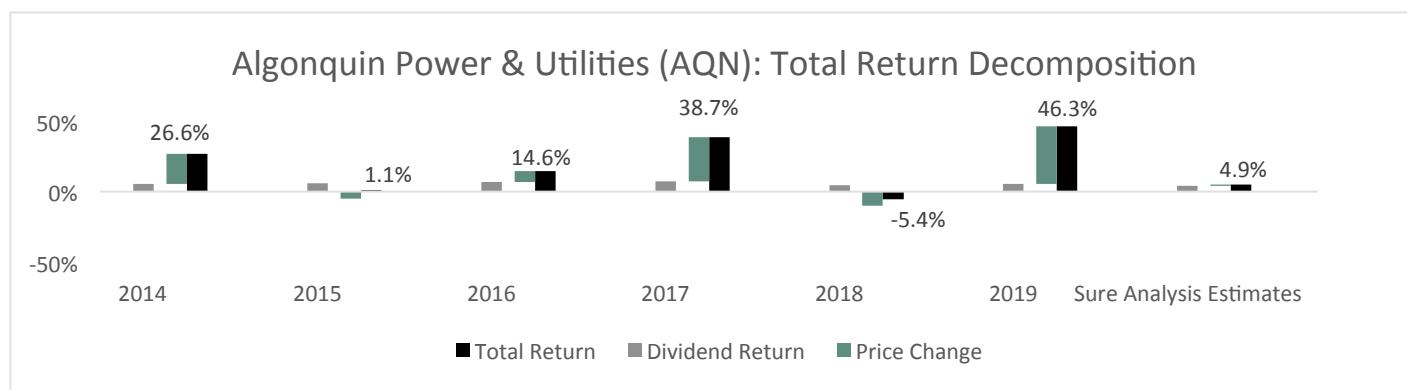
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	114%	117%	207%	127%	100%	107%	131%	105%	77%	87%	93%	90%

Algonquin cut its dividend during the last recession as earnings fell drastically. Most of the decade displayed payout ratios that were extended. That said, its earnings have been much more stable so far through this recession thanks to most of its operations being either regulated or having long-term contracts. Its payout ratio has also reduced to the 90% range, after aligning the company's U.S. dollar reporting to its U.S. dollar-denominated dividend. Going forward, it'd be more prudent for the company to further lower its payout ratio by growing its dividend at a slower pace than its earnings growth. Therefore, we estimate a 6% dividend growth rate versus an estimated EPS growth rate of 6.5%. Algonquin is awarded an investment-grade S&P credit rating of BBB.

Final Thoughts & Recommendation

Algonquin is a higher-risk utility due to its higher payout ratio but offers above-average growth in the space. The stock is overvalued. Over the next five years, we estimate total returns of 4.9%, coming from a forward yield of 3.9%, a decline of -5.4% from P/E contraction, and earnings growth of 6.5% per year. Because of low estimated returns, we rate the security as a sell. Investors should seek better opportunities in the Sure Dividend coverage universe for higher income and returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	180	265	351	634	811	741	815	1522	1648	1625
Gross Profit	85	195	230	379	449	469	596	1129	1164	1182
Gross Margin	47.1%	73.7%	65.5%	59.7%	55.3%	63.3%	73.1%	74.2%	70.6%	72.7%
SG&A Exp.	15	17	20	22	30	29	34	59	53	57
D&A Exp.	49	46	52	93	99	109	146	257	261	284
Operating Profit	21	53	42	97	119	131	174	368	378	369
Operating Margin	11.9%	19.8%	12.0%	15.3%	14.7%	17.7%	21.4%	24.2%	23.0%	22.7%
Net Profit	18	23	15	19	65	85	97	149	185	531
Net Margin	10.0%	8.6%	4.2%	3.0%	8.0%	11.4%	11.9%	9.8%	11.2%	32.7%
Free Cash Flow	21	9	-15	-56	-206	42	-88	-239	64	30
Income Tax	-21	-22	-14	9	14	32	28	73	53	70

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	1017	1256	2793	3265	3534	3597	6138	8396	9399	10911
Cash & Equivalents	5	71	53	13	8	90	82	43	47	62
Accounts Receivable	26	43	89	151	162	135	141	245	246	259
Inventories	0	3	24	31	27	21	28	89	96	91
Goodwill & Int. Ass.	75	64	119	131	126	133	276	1005	1009	1079
Total Liabilities	677	715	1384	1888	1952	1946	4288	5075	5701	6505
Accounts Payable	2	8	34	14	59	36	67	120	90	150
Long-Term Debt	442	446	776	1179	1095	1071	3178	3080	3337	3932
Shareholder's Equity	340	504	805	788	1125	1240	1272	2533	2993	3691
D/E Ratio	1.30	0.88	0.84	1.31	0.84	0.77	2.22	1.13	1.05	1.01

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	1.8%	2.0%	0.7%	0.6%	1.9%	2.4%	2.0%	2.1%	2.1%	5.2%
Return on Equity	5.0%	5.4%	2.2%	2.4%	6.8%	7.2%	7.8%	7.9%	6.7%	15.9%
ROIC	2.3%	2.6%	0.9%	0.8%	2.5%	3.1%	2.5%	2.6%	2.8%	6.9%
Shares Out.	94.34	116.96	158.91	205.83	216.34	256.52	274.08	385.99	466.05	504.74
Revenue/Share	1.91	2.27	2.21	3.08	3.75	2.89	2.98	3.94	3.54	3.22
FCF/Share	0.22	0.07	-0.09	-0.27	-0.95	0.16	-0.32	-0.62	0.14	0.06

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

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