Hannon Armstrong Sustainable Infr. (HASI)

Updated November 8th, 2020 by Nikolaos Sismanis

Key Metrics

Current Price:	$47.2	**5 Year CAGR Estimate:**	7.2%	**Market Cap:**	$3.51B
Fair Value Price:	$37.0	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date:**	12/24/2020
% Fair Value:	128%	**5 Year Valuation Multiple Estimate:**	-4.8%	**Dividend Payment Date:**	01/08/2021
Dividend Yield:	2.9%	**5 Year Price Target**	$60	**Years Of Dividend Growth:**	2
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	1.49%

Overview & Current Events

Hannon Armstrong is a U.S. public company entirely committed to investments in climate change solutions, providing capital to leading companies in energy efficiency, renewable energy, and other sustainable infrastructure markets. The company's portfolio of assets is worth around $2.2 billion and is split between three market segments: Its Behind-the-Meter business (59% of assets) focuses on the installation of solar power, electric storage, and other heat and power systems. The Grid-Connected segment (40% of assets) involves investments in grid-connected renewable energy projects, such as solar and off/on-shore wind projects, whose generated yield the company then sells on the wholesale energy markets. Finally, while currently occupying around 1% of its portfolio, the company invests in Sustainable Infrastructure projects, enabling the use of natural resources, such as its projects to slow pollution runoff across the Chesapeake Bay region. Hannon Armstrong has around 208 investments, with a weighted average life of 16 years and an investment yield of around 7.7%. The company generates around $100 million in annual revenues, is based in Annapolis, Maryland, and has chosen to qualify itself as a REIT due to the physical nature of its assets.

On November 5th, Hannon Armstrong reported its Q3 results for the period ending September 30th, 2020. Revenues grew by 25% to $22.5 million, while EPS[1] came in at $0.78, compared to $0.54 during Q3-2019. The higher top and bottom line was primarily the result of HASI's portfolio expansion, as the company keeps on capitalizing on the favorable ESG market conditions. With a hungry market for green assets, management raised over $500 million through a 10-year bond with a 3.75% coupon and a convertible 3-year 0% bond. With such cheap financing and the highest-ever global demand for renewables, the company's future pipeline consists of $2.5 billion worth of upcoming infrastructure assets, which should keep HASI's steady growth trajectory robust.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	---	---	---	-$0.68	$0.43	$0.21	$0.32	$0.57	$0.75	$1.25	***$1.48***	***$2.38***
DPS	---	---	---	$0.42	$0.92	$1.08	$1.23	$1.32	$1.32	$1.34	***$1.36***	***$1.50***
Shares[2]	---	---	---	15.7	20.7	30.8	40.3	50.4	52.8	63.9	***67.6***	***120.0***

HASI's EPS has been growing rapidly, in line with its asset portfolio. We expect the company to keep taking advantage of the cheap financing available for green assets to keep growing rapidly. We estimate a medium-term EPS growth of around 10% to reasonably price in some slowdown in its operations, as well as the potential dilution amid its share issuances and convertible bonds materializing. To keep investors satisfied and the stock high enough to successfully issue funds through shares issuances, management would pay shareholders dividends through its debt proceeds, as the company was on its way to profitability. At its past dividend yields of around 4%-6% indicates, its cost of equity was lower than its investment yield (~7.7%), and hence its growth strategy was viable. EPS recently caught up to its distributions, self-funding the dividend. Still, as management widens its coverage ratio and self-funds future projects, we expect DPS to grow by around 2% in the medium term.

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[1] While a REIT, HASI's assets are not (yet) subject to any meaningful depreciation/amortization. Hence it reports in EPS over FFOs.
[2] Share count is in millions.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	---	---	---	---	32	90	68	43	35	32.0	***31.9***	***25.0***
Avg. Yld.	---	---	---	4.8%	6.1%	6.3%	5.7%	6.0%	6.6%	4.6%	***2.9%***	***2.5%***

HASI's historical P/E ratio reflects the market's expectations for the company's rapid EPS growth, hence the prolonged premium. While we expect the company's expansionary phase to continue unfolding as the shift towards renewables evolves, we expect shares to eventually settle to a more reasonable multiple, around 25 times its underlying earnings. In terms of its dividend yield, the figure would hover around 4%-6% as payouts were derived out of debt, and the company had yet to prove that its risky strategy would quickly achieve dividend coverage. With profitability snowballing due to the global ESG boost over the past couple of years, dividend coverage is secure. Rushing to capture HASI's, now safe distributions, and juicy growth prospects, shares have undergone a huge rally, currently yielding just under 3%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

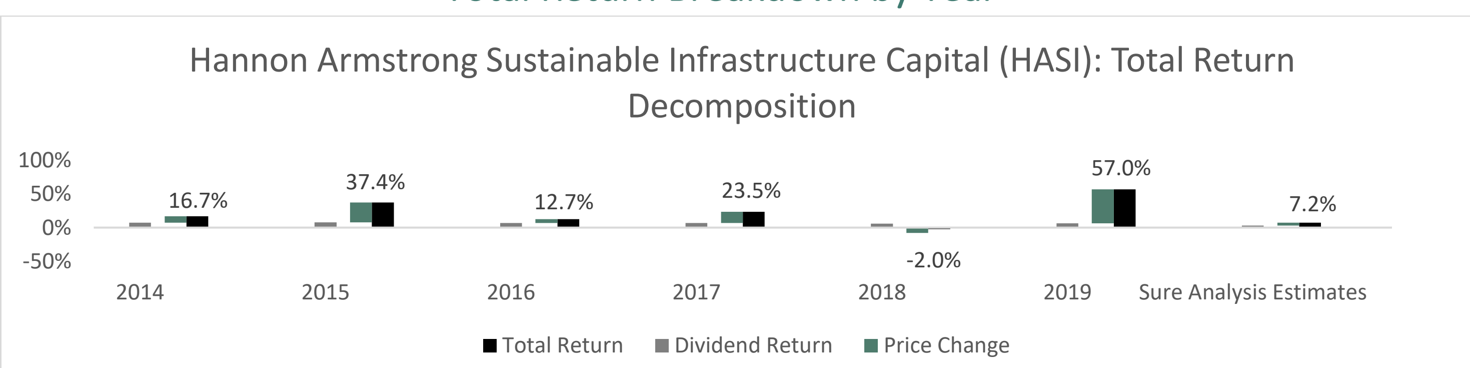
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	--	--	--	--	214%	514%	384%	231%	176%	107%	92%	***63%***

HASI's risky distribution strategy has paid off, and the dividend should now be quite safe, though not growing as fast. The company's competitive advantage includes a leading market position in a relatively new and booming industry and a global push for renewables, which should ensure a long-term rich backlog and ultra-low financing, further boosting its ROI. It's also worth mentioning that 86% of its Board of Directors is independent, while its management is not composed of just the usual Ivy League MBA executives, but also holds various distinctions such as CPAs and CFAs, equipped with the skills to pull off some complex financial engineering, including HASI's early financing strategy. Based on an extremely favorable industry outlook and HASI's robust pipeline and cheap financing, we believe that the company will keep performing well and is unlikely to face any challenges correlated to the underlying economy.

Final Thoughts & Recommendation

Hannon Armstrong is one of the leading diversified renewable energy asset operators, despite its small market cap. Management has proven its skills in terms of rapidly growing HASI's infrastructure portfolio, while adequately rewarding shareholders during the same time, resulting in market-beating returns. The market has recently captured the majority of the stock's yield surplus. Still, we believe that current investors are looking at a fruitful investment case, at a booming sector boosted by the current socio-political environment, even though our expected annualized returns of around 7.3% are more humble than its historical ones. We rate shares a hold at current prices.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	15.3	2.0	15.4	14.3	26.2	32.2	42.1	62.8	84.7	141.5
SG&A Exp.	9.0	2.5	3.9	3.8	5.9	7.3	8.3	11.2	15.1	14.7
D&A Exp.	3.8	1.0	0.4	1.1	2.6	4.0	7.7	3.6	4.5	3.6
Net Profit	14.1	-5.0	3.8	-10.5	9.6	8.0	14.7	30.9	41.6	81.6
Net Margin	91.8%	-257%	24.7%	-73.3%	36.7%	24.7%	34.8%	49.1%	49.1%	57.6%
Free Cash Flow	7.2	1.5	9.7	-10.8	5.1	18.5	56.9	11.7	58.8	29.5
Income Tax	---	0.0	0.0	-0.3	0.0	0.1	0.1	0.9	2.1	8.1

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	---	175	232	571	1009	1470	1746	2250	2155	2387
Cash & Equivalents	---	2	21	32	58	43	29	57	21	6
Total Liab.	---	158	213	421	735	1038	1172	1607	1350	1447
Accounts Payable	---	2	8	9	11	18	25	26	37	54
Long-Term Debt	0	155	205	337	635	911	975	1428	1242	1393
Total Equity	---	16	19	147	269	428	571	639	801	936
D/E Ratio	---	9.5	10.7	2.3	2.4	2.1	1.7	2.2	1.6	1.5

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	---	---	1.9%	-2.6%	1.2%	0.6%	0.9%	1.5%	1.9%	3.6%
Return on Equity	---	---	21.5%	-12.6%	4.6%	2.3%	2.9%	5.1%	5.8%	9.4%
ROIC	---	---	1.9%	-2.9%	1.4%	0.7%	1.0%	1.7%	2.0%	3.7%
Shares Out.	15.1	15.1	15.1	15.7	20.7	30.8	40.3	50.4	52.8	64.8
Revenue/Share	1.01	0.13	1.02	0.91	1.27	1.05	1.04	1.25	1.60	2.18
FCF/Share	0.48	0.10	0.64	-0.68	0.25	0.60	1.41	0.23	1.11	0.46

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