



Canadian Utilities (CDUAF)

Updated April 29th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$28	5 Year CAGR Estimate:	12.5%	Market Cap:	\$7.63B
Fair Value Price:	\$30	5 Year Growth Estimate:	4.0%	Ex-Dividend Date:	05/05/2021
% Fair Value:	93%	5 Year Valuation Multiple Estimate:	1.5%	Dividend Payment Date¹:	06/01/2021
Dividend Yield:	5.1%	5 Year Price Target	\$36	Years Of Dividend Growth¹:	48
Dividend Risk Score:	B	Retirement Suitability Score:	A	Last Dividend Increase:	1.1%

Overview & Current Events

Canadian Utilities is a \$7.63 billion company with approximately 5,000 employees. ATCO owns 52% of Canadian Utilities. Based in Alberta, Canadian Utilities is a diversified global energy infrastructure corporation delivering solutions in Electricity, Pipelines & Liquid, and Retail Energy. The company prides itself on having Canada's longest consecutive years of dividend increases, with a 48-year streak. Unless otherwise noted, US\$ is used in this research report.

Canadian Utilities reported its Q1-2021 results for the period ended March 31st, on April 29th, 2021. Revenues and EPS for the year amounted to \$738 million and \$0.54, indicating an increase of 2.4% and 45.9%, respectively, in constant currency terms.

Stable revenues reflected the company's durable business model, which enjoys rising annual rates, helping boost results over time. The massive hike in net income was attributed to profitably normalizing. In the comparable period last year, the company had to take one-off, extraordinary costs (e.g., increased transmission costs) as a result of the initial COVID-19 outbreak. Earnings were also boosted by cost efficiencies, growth in asset base, and a long-term contract to operate Puerto Rico's electricity transmission and distribution system. Finally, the company benefited from increased demand for natural gas storage services and recovered business development costs in its Energy Infrastructure segment.

Due to profitably recovering faster than our previous expectations, we hike our FY2021 EPS estimate at \$2.00. Our forecast is also boosted by the ongoing depreciation of USD against the CAD, from which U.S.-based investors currently benefit. The stock's annualized dividend rate of C\$1.76 should translate to around US\$1.43 at the current FX rates.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$1.80	\$2.04	\$1.97	\$2.18	\$0.81	\$1.54	\$1.32	\$1.53	\$2.50	\$1.05	\$2.00	\$2.43
DPS	\$0.79	\$0.89	\$0.91	\$0.92	\$0.85	\$0.97	\$1.14	\$1.15	\$1.30	\$1.38	\$1.43	\$1.62
Shares²	252	255	255	258	262	265	267	269	272	325	330	380

By benefiting from a stable business model, Canadian Utilities can slowly but progressively grow its earnings. The company consistently invests in new projects and benefits from the base rate increases, which grow at around 3% to 4% annually. During Q1, management filed an application with the Alberta Utilities Commission to postpone Canadian Utilities' electricity and natural gas distribution rate increases for 2021 and collect the deferred amounts beginning in 2023 to assist the local communities. Combining the company's growth projects, the potential for modest margin improvements but –as voluntarily pursued– postponed rate base increases, we lower our expected growth rate from 5% annually to 4%. Our DPS CAGR estimate remains at 2.5%. The company will likely improve its payout ratio before its new projects start producing enough cash flows to re-accelerate dividend growth. U.S. investors have enjoyed a lesser growth in their dividends than the Canadian ones over the past decade due to the depreciation of \$CAD to \$USD.

¹ Estimated dividend dates; Years of Dividend Growth and Last Dividend Increase based in C\$.

² Share count is in millions.

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Regardless, the stock's impressive 10-year dividend CAGR of 9.6% is more than enough to compensate for the FX fluctuations, progressively growing investors' income.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	12.8	16.4	17.5	18.1	19.3	20.9	18.3	18.2	15.0	22.9	14.0	15.0
Avg. Yld.	3.0%	2.7%	2.7%	2.7%	3.4%	3.6%	3.5%	4.6%	4.8%	4.8%	5.1%	4.4%

Canadian Utilities' shares are currently offer a generous dividend yield of 5.1%, offering attractive tangible returns in the form of quarterly income. The yield is also currently at the higher-end of the stock's historical range, which makes this Canadian Utilities the most attractive it has even been in decades from an income standpoint. The stock's current P/E ratio of around 14 is notably lower than its historical average. Considering the company's stability in operations and hefty dividend yield, we can see the stock's valuation multiple slightly expanding towards 15 in the medium-term. Approaching half a century of consecutive annual increases, we believe that the high yield will attract investor interest and consider our projected valuation multiple quite a safe bet.

Safety, Quality, Competitive Advantage, & Recession Resiliency

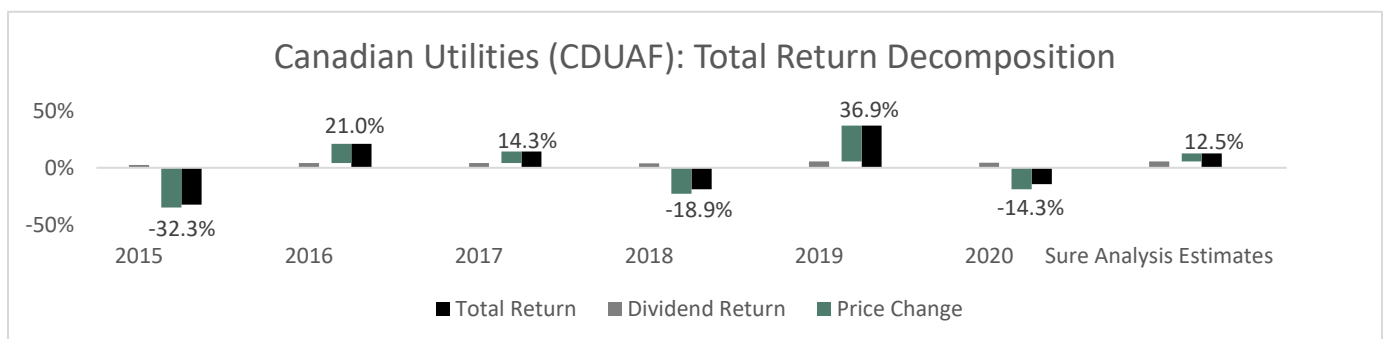
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Payout	44%	44%	46%	42%	105%	63%	86%	75%	52%	131%	72%	66%

The company's competitive advantage lies in the moat regulated utilities are surrounded by. With no easy entry in the sector, regulated utilities enjoy an oligopolistic market with little competition threat. The company's resiliency has been proven for decade after decade. Despite multiple recessions and uncertain environments over the past 48 years, the company has withstood every one of them while raising its dividend. While Canadian Utilities' payout ratio went under pressure during 2020 (though dividends were in reality covered from its operating cash flows if we are to exclude depreciation and amortization,) by 2026 we expect it to have returned to much more comfortable levels, just over 65% of its net income.

Final Thoughts & Recommendation

We believe that Canadian Utilities is an excellent buy for income-oriented investors who seek stable and predictable returns. The latest dividend increase of 1.1% in local currency may indicate a slowdown compared to its 5-year average of 6.3%. However, as the company retains more cash to invest in future projects and pay down its debt, the dividend yield remains very attractive. We believe that Canadian Utilities offers low volatility and a stable investment case during a time of sky-high valuations. We project medium-term returns of around 12.5%, powered by the stock's high yield and modest EPS & DPS growth expectations. We rate the stock a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	\$3,033	\$3,040	\$3,283	\$3,261	\$2,557	\$2,567	\$3,152	\$3,378	\$2,942	\$2,413
Gross Profit	\$2,018	\$2,104	\$2,266	\$2,137	\$1,910	\$2,009	\$2,144	\$2,240	\$2,188	\$1,877
Gross Margin	66.5%	69.2%	69.0%	65.5%	74.7%	78.3%	68.0%	66.3%	74.4%	77.8%
SG&A Exp.	\$446	\$497	\$498	\$463	\$363	\$293	\$272	\$330	\$258	\$255
D&A Exp.	\$374	\$412	\$464	\$466	\$503	\$433	\$461	\$492	\$439	\$455
Operating Profit	\$942	\$943	\$1,033	\$922	\$639	\$898	\$917	\$835	\$963	\$702
Operating Margin	31.0%	31.0%	31.5%	28.3%	25.0%	35.0%	29.1%	24.7%	32.7%	29.1%
Net Profit	\$521	\$553	\$570	\$644	\$276	\$468	\$397	\$489	\$717	\$319
Net Margin	17.2%	18.2%	17.4%	19.8%	10.8%	18.2%	12.6%	14.5%	24.4%	13.2%
Free Cash Flow	-\$14	-\$870	-\$517	-\$596	-\$43	\$248	\$73	-\$205	\$185	\$553
Income Tax	\$189	\$156	\$182	\$187	\$161	\$178	\$133	\$174	\$40	\$113

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	11,248	13,287	14,135	14,388	13,021	13,945	16,572	16,020	15,344	15,920
Cash & Equivalents	\$574	\$351	\$468	\$302	\$350	\$256	\$304	\$400	\$745	\$609
Accounts Receivable	\$399	\$533	\$448	\$418	\$312	\$384	\$469	\$496	\$389	\$426
Inventories	\$77	\$79	\$85	\$73	\$32	\$28	\$32	\$23	\$23	\$22
Goodwill & Int. Ass.	\$285	\$331	\$347	\$341	\$349	\$390	\$448	\$463	\$482	\$514
Total Liabilities	\$7,148	\$8,890	\$9,070	\$9,558	\$8,558	\$9,294	\$11,530	\$11,202	\$10,046	\$10,580
Long-Term Debt	\$4,468	\$5,502	\$5,910	\$6,305	\$5,759	\$6,214	\$7,890	\$7,694	\$6,864	\$7,102
Shareholder's Equity	\$3,391	\$3,670	\$4,019	\$3,870	\$3,259	\$3,401	\$3,714	\$3,592	\$4,020	\$4,029
D/E Ratio	1.09	1.25	1.17	1.31	1.33	1.38	1.61	1.64	1.33	1.37

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	5.1%	4.5%	4.2%	4.5%	2.0%	3.5%	2.6%	3.0%	4.6%	2.0%
Return on Equity	15.7%	15.7%	14.8%	16.3%	7.7%	14.1%	11.1%	13.4%	18.8%	7.9%
ROIC	6.6%	6.0%	5.5%	5.8%	2.6%	4.4%	3.3%	3.8%	5.8%	2.6%
Shares Out.	255.4	256.0	259.3	262.8	265.3	267.8	270.1	272.1	273.2	273
Revenue/Share	\$11.88	\$11.87	\$12.66	\$12.41	\$9.64	\$9.59	\$11.67	\$12.41	\$10.77	\$8.83
FCF/Share	-\$0.06	-\$3.40	-\$1.99	-\$2.27	-\$0.16	\$0.93	\$0.27	-\$0.75	\$0.68	\$2.02

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

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