



Canadian Utilities (CDUAF)

Updated November 2nd, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$29	5 Year CAGR Estimate:	11.7%	Market Cap:	\$7.86B
Fair Value Price:	\$29	5 Year Growth Estimate:	4.0%	Ex-Dividend Date:	11/03/2021
% Fair Value:	102%	5 Year Valuation Multiple Estimate:	-0.3%	Dividend Payment Date:	12/01/2021
Dividend Yield:	4.8%	5 Year Price Target	\$35	Years Of Dividend Growth¹:	49
Dividend Risk Score:	B	Retirement Suitability Score:	A	Last Dividend Increase:	1.1%

Overview & Current Events

Canadian Utilities is a \$7.86 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 49-year streak. Unless otherwise noted, US\$ is used in this research report.

On October 28th, 2021, Canadian Utilities reported its Q3-2021 results for the period ending September 30th. Revenues and EPS for the quarter amounted to \$636.8 million and \$0.27 per share, indicating an increase of 8.8% and 17.8%, respectively, in constant currency terms.

Higher revenues were mainly due to improved performance at ATCO energy resulting from higher electricity and natural gas commodity prices associated with floating rate energy contracts. The growth in EPS was mainly due to higher earnings from the International Electricity Operations business and also due to the stabilization of inflation in Australia, which positively impacted earnings in the International Natural Gas Distribution business.

Following the company's Q3 results, we retain our expectations for a FY2021 EPS of \$1.80. Our forecast also takes into account the ongoing depreciation trend 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\$1.41 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	\$1.80	\$2.19
DPS	\$0.79	\$0.89	\$0.91	\$0.92	\$0.85	\$0.97	\$1.14	\$1.15	\$1.30	\$1.38	\$1.41	\$1.60
Shares²	252	255	255	258	262	265	267	269	272	272	270	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. In Q1, management had filed an application with the Alberta Utilities Commission to postpone Canadian Utilities' electricity and natural gas distribution rate increases for 2021. The company expects to receive the deferred revenues in early 2022. Combining the company's growth projects, the potential for modest margin improvements, and –as voluntarily pursued, – the postponed rate base increases, we retain our expected growth rate at 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. 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.

¹ Years of Dividend Growth and Last Dividend Increase based in C\$.

² Share count in millions

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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	16.3	16.0
Avg. Yld.	3.0%	2.7%	2.7%	2.7%	3.4%	3.6%	3.5%	4.6%	4.8%	4.8%	4.8%	4.6%

Canadian Utilities' shares are currently attached to a juicy dividend yield of 4.8%, 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 legendary dividend payer the most attractive it has even been in decades from an income standpoint. The stock's current P/E ratio of around 16.3 is notably lower than its historical average. Considering the company's limited earnings growth expectations in the medium term, we can see the stock's valuation multiple remaining at its current low levels. However, due to approaching half a century of consecutive annual increases, the high yield is more than likely to attract investor interest going forward. Hence, we don't expect the multiple to be compressed any further.

Safety, Quality, Competitive Advantage, & Recession Resiliency

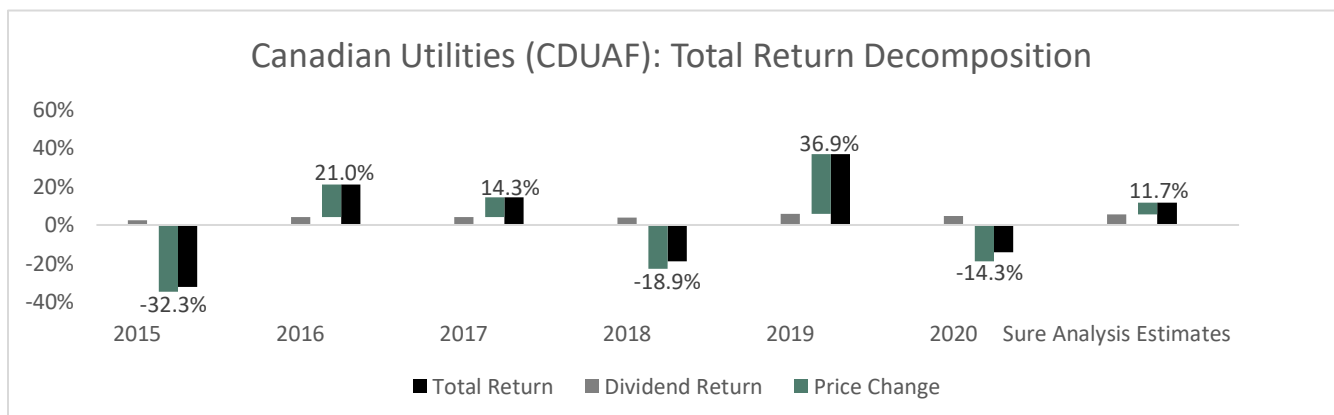
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Payout	44%	44%	46%	42%	105%	63%	86%	75%	52%	131%	78%	73%

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 49 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 70% 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 debts, 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 11.7%, powered by the stock's juicy 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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