



Global Water Resources (GWRS)

Updated November 13th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$18.50	5 Year CAGR Estimate:	-1.0%	Market Cap:	\$419.0 M
Fair Value Price:	\$15.00	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	11/15/2021
% Fair Value:	154%	5 Year Valuation Multiple Estimate:	-8.3%	Payment Date:	11/30/2021
Dividend Yield:	1.6%	5 Year Price Target	\$16.06	Years Of Dividend Growth:	6
Dividend Risk Score:	F	Retirement Suitability Score:	F	Last Dividend Increase:	0.7%

Overview & Current Events

Global Water Resources is a water resource management company that owns, operates, and manages regulated water, wastewater, and recycled water utilities primarily in metropolitan Phoenix, Arizona. The \$419 million market-cap company serves more than 61,000 people in 23,000 homes. Global Water generates around \$40 million in annual revenues and pays its dividends on a monthly basis.

On November 8th, 2021, Global Water reported its Q3-2021 results for the period ending September 30th, 2021. Revenues increased by 6.0 % year-over-year to \$11.4 million. The increase was driven primarily by a \$0.7 million recognition of revenue under infrastructure coordination and financing agreements (ICFAs), as well as growth in connections and rates. EPS came in at just \$0.07, compared to \$0.05 last year, as Global Water has been reinvesting the entirety of its profits, maintaining a razor-thin (or even negative) bottom line. Global Water is tapping into the fragmented State of Arizona, which is currently the U.S.'s fastest homeownership growth state – hence the consistent organic growth. Total active connections grew by 9.2% to 51,958 compared to the prior-year period, primarily due to growth in its service areas. The company continues to pursue accretive acquisitions with consolidation benefits and expects continuous growth in connections and rates.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	---	---	---	---	---	(\$0.13)	\$0.23	\$0.15	\$0.10	\$0.05	\$0.40	\$0.54
DPS	---	---	---	---	---	0.26	0.27	\$0.28	\$0.29	\$0.29	\$0.29	\$0.32
Shares¹	---	---	---	---	---	19.1	19.6	20.5	21.5	22.5	22.6	28.5

Global Water has many tailwinds including considerable growth in its recycled water deliveries (7.6% growth YoY), massive rate increases (requested 13.4% rate increase through 2022), and the solid population growth in Phoenix (17.81% since 2010). As such, we expect EPS to expand massively when expansionary investments slow down. To reflect the stock's actual EPS potential, effectively excluding its current capital-intensive investments, we have used underlying earnings power of \$0.40, growing by a rate of 6% annually through 2026. Note that this is a 'potential' figure, rather than something that's likely to materialize this year. In terms of its dividend, the company uses a complex financing strategy. Since the underlying net income does not cover dividends, management had been consistently issuing shares and using the proceeds to pay the monthly dividend. In a sense, the monthly dividend plays the role of interest paid to shareholders for "lending" their funds to the company. While this strategy would not be sustainable in the long-term, the company expects to see significant EPS growth over the next few years, as its growth eventually matures and net income catches up to the dividends paid. Management has been growing the dividend annually by fractions (0.7%) as a token to shareholders for their patience as the company drains its margins in order to grow. Consequently, we expect DPS to continue growing by no more than an annualized 2% in the medium term. Not only can Global Water not afford it, but to issue additional shares at a faster rate would be arguably too dangerous to pull-off under its already quite complex financing strategy.

¹ Share count is 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.



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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	---	---	---	---	---	---	---	---	---	---	46.3	30.0
Avg. Yld.	---	---	---	---	---	1.3%	2.8%	2.8%	2.7%	1.9%	1.6%	2.0%

The company's past P/E ratios are not meaningful due to management's strategy mentioned above. As its EPS catches up, we expect the stock's valuation to settle around 30 times earnings, which is consistent with the rest of the industry. This valuation multiple could be too rich, though we consider it reasonable as investors appreciate the secured cash flows that come from water being an essential utility and the regulatory rate increases. While a P/E of 30 in the future may be reasonable, the current P/E of 46.3 on our earnings power is beyond rich. We consider shares quite expensive at their current levels. Shares offer a dividend yield of around 1.6%, which has been pushed lower amid the stock's massive, rather unjustifiable rally. We expect the yield to increase amid a potential valuation correction over time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

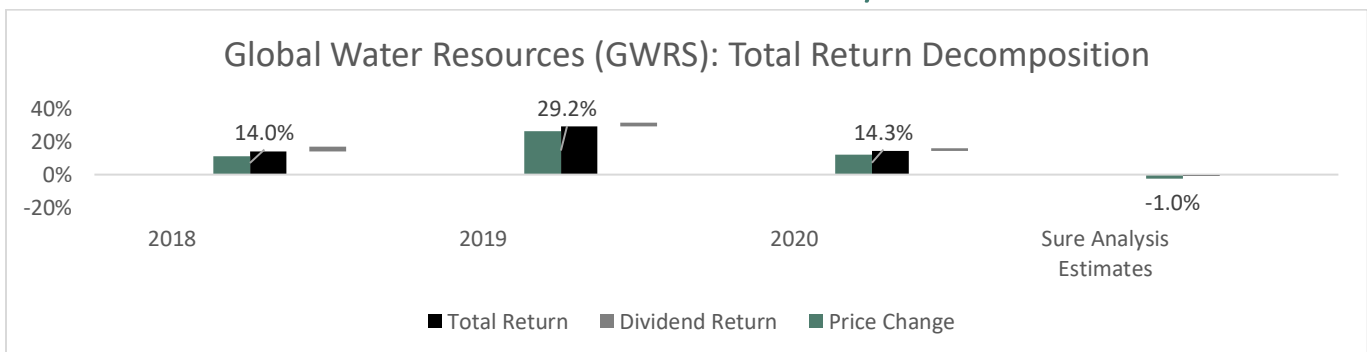
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	---	---	---	---	---	117%	185%	288%	576%	72%	60%

To claim that Global Water's dividends are safe would be reckless. Management is leveraging its business's ultra-secure cash flows to make this work, and while it is currently working, payout safety is largely speculative. The company's strategy of issuing shares in order to pay dividends is not exactly a textbook financing case. Still, the company is growing in one of the most attractive cities, benefiting from robust organic growth and the industry's stability. We believe that the company is subject to minor operational risks and should continue expanding. Its history as a trading company is not that long, however cash flows should remain robust even under a heavy recession. Further, the company should not face significant competition going forward, as water provision is a regulated capital-intensive business.

Final Thoughts & Recommendation

Global Water is a truly unique case. The company is benefiting from several catalysts, including organic growth amid operating in one of America's fastest-growing areas. Consequently, the company is able to request massive rate increases while enjoying robust cash flows due to its business model. However, management's financing strategy may be too exotic for some investors. Since our expected EPS forecast is quite speculative, our expected returns remain quite speculative as well. As more quarters pass by, our estimates should grow more accurate. In any case, we are currently estimating there are no gains to be made over the next few years, as investors have clearly overvalued the company. We rate share a sell at their current price levels.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	---	---	---	33	32	30	31	36	35	38.6
Gross Profit	---	---	---	22	23	22	24	27	27	29.1
Gross Margin	---	---	---	68.0%	71.0%	73.0%	75.8%	76.8%	74.9%	75.4%
SG&A Exp.	---	---	---	9	8	10	9	11	11	12.7
D&A Exp.	---	---	---	9	8	6	7	7	8	9
Operating Profit	---	---	---	55	7	6	7	9	7	7.3
Operating Margin	---	---	---	168.3%	20.4%	19.5%	23.5%	26.1%	19.6%	18.9%
Net Profit	---	---	---	65	21	(3)	5	3	2	1.1
Net Margin	---	---	---	199.4%	66.9%	-8.4%	14.6%	8.7%	6.3%	2.8%
Free Cash Flow	---	---	---	10	1	(7)	(10)	7	0	5.4
Income Tax	---	---	---	(17)	21	(1)	(1)	2	1	0.8

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	---	---	---	308	236	239	239	262	266	283
Cash & Equivalents	---	---	---	7	12	20	5	13	8	18
Accounts Receivable	---	---	---	1	1	1	2	1	2	2.5
Inventories	---	---	---	---	---	---	---	---	---	---
Goodwill & Int. Ass.	---	---	---	26	13	13	13	16	17	16
Total Liabilities	---	---	---	280	216	224	224	235	241	251
Accounts Payable	---	---	---	2	1	2	0	1	1	0.5
Long-Term Debt	---	---	---	130	104	114	114	114	114	114
Shareholder's Equity	---	---	---	28	20	15	15	28	25	32
D/E Ratio	---	---	---	4.69	5.19	7.62	7.70	4.11	4.64	3.56

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	---	---	---	---	7.9%	-1.1%	1.9%	1.2%	0.8%	
Return on Equity	---	---	---	---	89.5%	-14.3%	30.5%	14.5%	8.5%	
ROIC	---	---	---	---	15.2%	-2.0%	3.5%	2.3%	1.6%	
Shares Out.	---	---	---	---	---	19.1	19.6	20.5	21.5	
Revenue/Share	---	---	---	1.68	1.65	1.56	1.59	1.73	1.65	
FCF/Share	---	---	---	0.51	0.05	(0.35)	(0.50)	0.32	0.02	

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

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