



SJW Group (SJW)

Updated November 2nd, 2021 by Nathan Parsh

Key Metrics

Current Price:	\$70	5 Year CAGR Estimate:	0.2%	Market Cap:	\$2.1 billion
Fair Value Price:	\$43	5 Year Growth Estimate:	7.6%	Ex-Dividend Date:	11/5/2021
% Fair Value:	162%	5 Year Valuation Multiple Estimate:	-9.1%	Dividend Payment Date:	12/1/2021
Dividend Yield:	1.9%	5 Year Price Target	\$63	Years Of Dividend Growth:	55
Dividend Risk Score:	A	Retirement Suitability Score:	B	Last Dividend Increase:	6.3%

Overview & Current Events

SJW Group is a water utility company that produces, purchases, stores, purifies and distributes water to consumers and businesses in the Silicon Valley area of California, and the area north of San Antonio, Texas. SJW Group has a small real estate division that owns and develops properties for residential and warehouse customers in California and Tennessee. The company generates about \$620 million in annual revenues. SJW Group completed its acquisition of Connecticut Water, formerly known as CTWS, on 10/9/2019.

SJW Group reported earnings results for the third quarter on 10/29/2021. Revenue grew 0.6% to \$166.9 million, but missed estimates by \$20 million. Earnings-per-share of \$0.64 compared negatively to \$0.96 in the prior year and was \$0.11 lower than expected.

The revenue gain was primarily due to a \$7.6 million increase in water rates, \$3.3. million in net recognition of certain regulatory mechanisms in the state of Connecticut and Maine as well as a \$1.8 million recognition of balancing and memorandum accounts. These gains were offset by a \$12.9 million decrease in customer usage. Water production expenses increased 3.4% to \$72.1 million. Operating expenses outside of water production costs were up 12.3% to \$61 million.

SJW Group is now expected to earn \$1.97 in 2021, up from \$1.92 previously.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$1.11	\$1.18	\$1.12	\$2.54	\$1.85	\$2.57	\$2.86	\$1.82	\$1.35	\$2.14	\$1.97	\$2.84
DPS	\$0.69	\$0.71	\$0.73	\$0.75	\$0.78	\$0.81	\$1.04	\$1.12	\$1.20	\$1.28	\$1.36	\$1.82
Shares¹	19	19	20	20	20	21	21	29	29	29	30	30

SJW Group's earnings-per-share often vary wildly from year to year, but earnings-per-share growth over the past 10 years is 7.6%, an impressive growth rate for a water utility. We estimate that the SJW Group will grow earnings at the average growth rate of the combined companies (7.6%) due to revenue growth and rate increases. In connection with the CTWS merger, SJW Group issued nearly 8 million new shares on 12/5/2018 in order to fund 50% of the proposed transaction, but we don't expect any significant additional dilution on the horizon.

SJW Group announced a 6.3% dividend increase for the 3/1/2021 payment, marking 55 consecutive years of growth for this Dividend King. SJW has a 10-year average growth rate of 4.8%. We expect dividends to grow at a rate of 6% annually through 2026.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	21.2	20.4	24.3	11.2	16.6	15.7	18.8	32.7	47.8	30.0	35.5	22.0
Avg. Yld.	2.9%	3.0%	2.7%	2.6%	2.5%	2.0%	1.9%	1.9%	1.9%	2.0%	1.9%	2.9%

¹ In millions of shares

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Price-to-earnings multiples for water utilities tend to be high, but SJW Group's multiple was extremely high in the 2018-2020 time period as it is today. The share price has increased \$1, or 1.4%, since our 8/9/2021 update. Using EPS estimates for the year, the stock trades with a forward P/E of 35.5. We maintain our 2026 target P/E of 22. If shares were to revert to this target P/E by 2026, then valuation would be a 9.1% headwind to annual returns over this period of time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

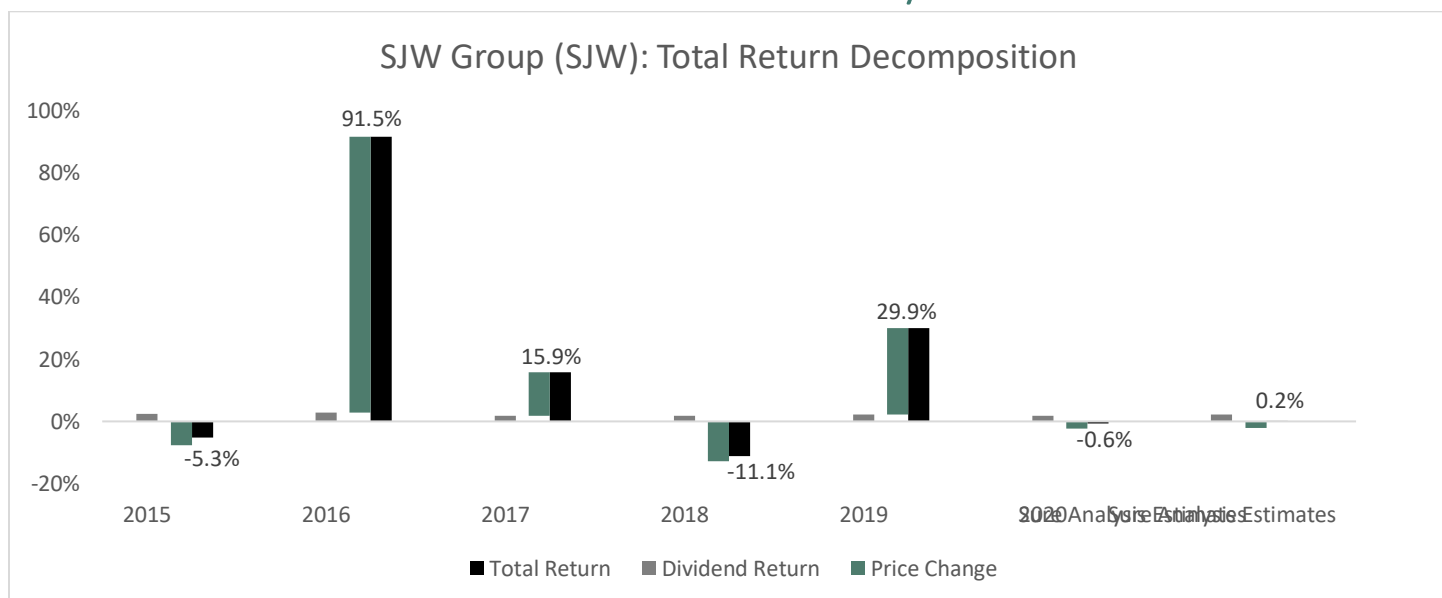
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	62%	60%	65%	30%	42%	32%	36%	62%	89%	60%	69%	64%

Many investors own utility companies for their reliable earnings and dividends, especially for uncertain economic times. During the last recession, SJW Group experienced a decline in earnings that took several years to recover. A key competitive advantage for SJW Group, aside from the concluded merger, is that it operates in two areas, Silicon Valley and Central Texas, that have seen high levels of population growth in recent years. These areas need improved water infrastructure to serve a growing client base, so local governments often allow the company to raise rates at a relatively high level in order to fund these projects. For example, SJW Group was approved for a 4.2% increase in 2018 for its customers in the Silicon Valley area. The company applied for rate increases of 9.8%, 3.7% and 5.2% over the next three years for this area. Investors should be aware of is that SJW Group's earnings are highly concentrated in California (60% of sales post Connecticut Water Service merger) and Connecticut (30% of sales post-merger).

Final Thoughts & Recommendation

After third quarter results, SJW Group is now projected to return 0.2% annually through 2026, which is up from our previous estimate of a 0% return. Projected returns stem from 7.6% earnings growth and a starting dividend yield of 1.9% that are nearly offset by a high single-digit valuation reversion. SJW Group had a solid third quarter even as water usage declined. The company faced a tough comparison as consumers spent more time at home last year during the third quarter in response to the COVID-19 pandemic. While we remain enthused about the business and the company's dividend growth track record, we find that the valuation leaves a lot to be desired. We have raised our 2026 price target \$2 to \$63, but continue to view shares of SJW Group as a sell due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	239	262	277	320	305	340	389	398	420	565
Gross Profit	134	141	142	182	179	196	213	211	224	317
Gross Margin	55.9%	53.9%	51.5%	57.1%	58.8%	57.6%	54.7%	52.9%	53.3%	56.1%
SG&A Exp.	39	43	44	41	47	42	49	49	66	80
D&A Exp.	33	35	37	39	42	46	51	57	68	92
Operating Profit	54	55	53	93	80	97	102	92	73	118
Operating Margin	22.8%	21.1%	19.3%	29.1%	26.2%	28.7%	26.2%	23.1%	17.4%	20.8%
Net Profit	21	22	22	52	38	53	59	39	23	62
Net Margin	8.7%	8.5%	8.1%	16.2%	12.4%	15.6%	15.2%	9.7%	5.6%	10.9%
Free Cash Flow	(7)	(32)	(34)	(38)	(12)	(31)	(51)	(57)	(53)	(111)
Income Tax	15	16	14	25	23	34	35	10	8	8

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	1,039	1,087	1,110	1,269	1,337	1,443	1,458	1,956	3,132	3,311
Cash & Equivalents	27	3	2	2	5	6	8	421	13	5
Accounts Receivable	13	12	14	15	16	16	17	19	36	47
Inventories	1	1	1							
Goodwill & Int. Ass.	10	11	18	14	16	24	14	17	662	663
Total Liabilities	775	813	789	909	954	1,022	995	1,067	2,242	2,394
Accounts Payable	7	8	13	7	16	19	23	25	35	34
Long-Term Debt	345	356	358	398	415	448	456	531	1,423	1,539
Shareholder's Equity	264	275	321	360	384	422	463	889	890	917
D/E Ratio	1.31	1.30	1.11	1.11	1.08	1.06	0.98	0.60	1.60	1.68

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	2.1%	2.1%	2.0%	4.4%	2.9%	3.8%	4.1%	2.3%	0.9%	1.9%
Return on Equity	8.0%	8.3%	7.5%	15.2%	10.2%	13.1%	13.4%	5.7%	2.6%	6.8%
ROIC	3.6%	3.6%	3.4%	7.2%	4.9%	6.3%	6.6%	3.3%	1.3%	2.6%
Shares Out.	19	19	20	20	20	21	21	29	29	29
Revenue/Share	12.71	13.88	13.86	15.66	14.87	16.50	18.82	18.64	14.72	19.67
FCF/Share	(0.39)	(1.72)	(1.68)	(1.84)	(0.60)	(1.51)	(2.48)	(2.67)	(1.85)	(3.87)

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

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