Otter Tail Corporation (OTTR)

Updated March 3rd, 2022 by Samuel Smith

Key Metrics

Current Price:	$60.7	**5 Year CAGR Estimate:**	8.1%	**Market Cap:**	$2.6B
Fair Value Price:	$75.8	**5 Year Growth Estimate:**	1.3%	**Ex-Dividend Date:**	5/14/22[1]
% Fair Value:	80%	**5 Year Valuation Multiple Estimate:**	4.6%	**Dividend Payment Date:**	6/10/22[2]
Dividend Yield:	2.7%	**5 Year Price Target**	$81	**Years Of Dividend Growth:**	9
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	5.4%

Overview & Current Events

Otter Tail Corporation goes back to 1907 with its electric utility, which was founded in Fergus Falls, MN. The company eventually expanded into metal fabrication and plastics manufacturing and today, it has about $1.2 billion in annual revenue split between utility, manufacturing and plastics operations. Otter Tail has a $2.6 billion market capitalization.

Otter Tail reported Q4 fiscal 2021 earnings on 2/14/22. Operating revenues increased 46.9% to $333.2 million year-over-year. Net income increased by a whopping 176.5% to $51.6 million from $18.7 million in the year-ago period. Diluted earnings-per-share came in at $1.23 per share, up from $0.45 per share year-over-year. The management also increased the quarterly common stock dividend to $0.4125 per share. Meanwhile, Otter Tail expects its 2022 diluted earnings per share to be in a range of $3.78 to $4.08.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$1.05	$1.37	$1.55	$1.56	$1.60	$1.86	$2.06	$2.15	$2.34	$4.23	***$3.79***	***$4.05***
DPS	$1.19	$1.19	$1.21	$1.23	$1.25	$1.28	$1.34	$1.40	$1.48	$1.56	***$1.65***	***$1.82***
Shares[3]	36.2	36.3	37.4	38.0	39.4	39.6	39.7	40.2	41.5	41.6	***41.6***	***42***

Otter Tail's earnings-per-share history has been fairly strong in the last decade, as earnings bottomed in 2010 and have grown every year since. We see average growth of 1.3% going forward after a strong jump up in expected earnings from 2020 to 2021. Otter Tail will achieve this growth via revenue increases from its utility business – which is looking stronger now that North Dakota and South Dakota have approved rate increases – as well as continued strong performances in its other two, non-utility lines of business. It continues to increase margins as well and the diversification it offers over other utilities is certainly a strength that is showing its value.

The company's manufacturing and plastics businesses have benefited from higher order rates as well as a lower income tax rate, while seeing gross margins tick higher over time. The higher operating expenses seen in prior quarters are uncharacteristic for Otter Tail, so we don't see any long-term impairment just yet.

We see all of these factors as continuing until further notice and as a result, earnings should grow steadily in the coming years. Otter Tail's full rate case in South Dakota is still pending, but the company has a favorable relationship with its regulators, so we are optimistic that Otter Tail will continue to receive the rate increases it needs to grow revenue.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	21.7	21.1	18.8	18.2	20.2	22.1	22.2	24.2	17.4	17.5	***16.0***	***20.0***
Avg. Yld.	5.2%	4.1%	4.2%	4.3%	3.9%	3.1%	2.9%	2.7%	3.6%	2.5%	***2.7%***	***2.2%***

[1] Estimate

[2] Estimate

[3] 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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The stock's price-to-earnings multiple has moved significantly lower in recent years after being artificially inflated due to low earnings-per-share from 2008 to 2011. However, today's multiple of 16.0 is below its recent historical norm of 20 and as such, we see the stock as undervalued.

We think shares will return to a multiple of roughly 20 over time, producing a nice tailwind to total returns moving forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	113%	87%	78%	79%	78%	69%	65%	65%	63%	43%	***44%***	***45%***

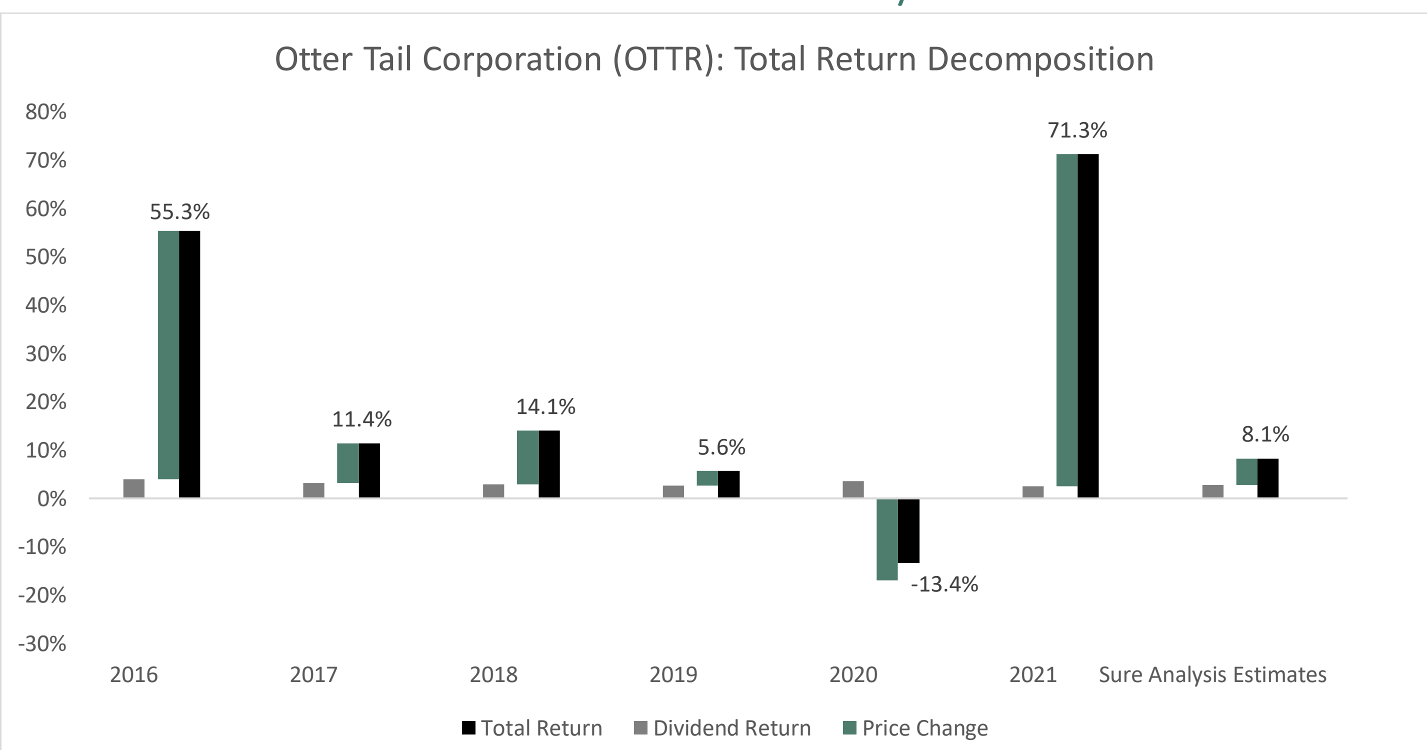
Otter Tail's payout ratio remains around two-thirds of earnings and we don't expect that will change. The company continues to boost its payout at roughly the same rate as earnings, so the dividend is quite safe and should continue to move higher over time.

Otter Tail's competitive advantage of having a diversified business model is also its disadvantage during recessions. The non-utility businesses are providing strong growth today but during the last recession, earnings fell much more than expected for a pure utility. That will likely happen next time there is a downturn, so investors should keep this in mind.

Final Thoughts & Recommendation

We see Otter Tail as a stock that offers 8.1% annualized total returns moving forward along with a safe 2.7% dividend yield that will grow with inflation over time. As a result, it is a solid holding for conservative dividend growth investors, and we rate it a Hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	710	743	799	780	804	849	916	920	890	1,197
Gross Profit	204	203	216	223	243	261	271	280	302	424
Gross Margin	28.7%	27.4%	27.0%	28.6%	30.2%	30.8%	29.6%	30.4%	33.9%	35.4%
D&A Exp.	58	58	58	60	73	73	75	78	82	91
Operating Profit	95	94	100	109	117	132	129	135	148	250
Operating Margin	13.3%	12.7%	12.5%	14.0%	14.5%	15.6%	14.1%	14.7%	16.6%	20.9%
Net Profit	(5)	51	58	59	62	72	82	87	96	177
Net Margin	-0.7%	6.8%	7.2%	7.6%	7.8%	8.5%	9.0%	9.4%	10.8%	14.8%
Free Cash Flow	119	(12)	(51)	(43)	2	41	38	(22)	(160)	59
Income Tax	7	13	17	22	20	27	15	17	20	36

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	1,602	1,596	1,741	1,819	1,912	2,004	2,053	2,274	2,578	2,755
Cash & Equivalents	52	2	-	-	-	16	1	21	1	2
Accounts Receivable	91	58	60	63	68	68	75	79	87	142
Inventories	69	73	85	85	84	88	106	98	92	148
Goodwill & Int. Ass.	53	44	43	55	53	51	50	49	48	47
Total Liabilities	1,065	1,061	1,168	1,214	1,242	1,307	1,324	1,492	1,707	1,764
Accounts Payable	88	96	107	89	89	85	96	121	121	135
Long-Term Debt	422	441	510	577	581	603	609	696	846	855
Shareholder’s Equity	522	535	573	605	670	697	729	781	871	991
LTD/E Ratio	0.78	0.82	0.89	0.95	0.87	0.87	0.84	0.89	0.97	0.86

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	-0.3%	3.2%	3.5%	3.3%	3.3%	3.7%	4.1%	4.0%	4.0%	6.6%
Return on Equity	-1.0%	9.6%	10.4%	10.1%	9.8%	10.6%	11.6%	11.5%	11.6%	19.0%
ROIC	-0.5%	5.3%	5.6%	5.2%	5.1%	5.7%	6.2%	6.2%	6.0%	9.9%
Shares Out.	36.2	36.3	37.4	38.0	39.4	39.6	39.7	40.2	41.5	41.6
Revenue/Share	19.60	20.45	21.75	20.70	20.75	21.37	22.97	23.01	21.76	28.62
FCF/Share	3.29	(0.33)	(1.39)	(1.13)	0.05	1.02	0.95	(0.56)	(3.90)	1.42

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