



Canadian Utilities (CDUAF)

Updated May 3rd, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	\$30	5 Year CAGR Estimate:	11.3%	Market Cap:	\$8.07 B
Fair Value Price:	\$28	5 Year Growth Estimate:	4.0%	Ex-Dividend Date:	05/04/2022
% Fair Value:	105%	5 Year Valuation Multiple Estimate:	-0.9%	Dividend Payment Date:	06/01/2022
Dividend Yield:	4.7%	5 Year Price Target	\$34	Years Of Dividend Growth¹:	50
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating	Buy

Overview & Current Events

Canadian Utilities is an \$8.07 billion company with approximately 5,000 employees. ATCO owns 53% 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 50-year streak. Unless otherwise noted, US\$ is used in this research report.

On April 27th, 2022, Canadian Utilities reported its Q1-2022 results for the period ending March 31st, 2022. Revenues and EPS for the quarter amounted to \$860 million and \$0.61 per share, indicating an increase of 22.3% and 41%, respectively, in constant currency terms.

Higher revenues were mainly the result of rate relief provided to customers in 2021 in light of the COVID-19 global pandemic and, subsequently, the decision to maximize the collection of 2021 deferred revenues in 2022. The growth in EPS was mainly due to the timing of operating costs in the Natural Gas Distribution business and earnings from International Electricity Operations. Elevated inflation levels positively impacted the International Natural Gas Distribution business's earnings, as well.

Our updated estimates point towards FY2022 EPS of \$1.77 (previously \$1.70). The company's current annualized dividend rate of C\$1.7768 equals close to US\$1.38 at the current FX rates.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$2.04	\$1.97	\$2.18	\$0.81	\$1.54	\$1.32	\$1.53	\$2.50	\$1.04	\$1.69	\$1.77	\$2.15
DPS	\$0.89	\$0.91	\$0.92	\$0.85	\$0.97	\$1.14	\$1.15	\$1.30	\$1.37	\$1.37	\$1.38	\$1.56
Shares²	255	255	258	262	265	267	269	272	272	270	269	350

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. Last year, management had filed an application with the Alberta Utilities Commission to postpone Canadian Utilities' electricity and natural gas distribution rate increases. 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	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	16.4	17.5	18.1	19.3	20.9	18.3	18.2	15.0	22.9	16.5	16.7	16.0
Avg. Yld.	2.7%	2.7%	2.7%	3.4%	3.6%	3.5%	4.6%	4.8%	4.8%	4.8%	4.7%	4.5%

Canadian Utilities' shares are currently attached to a juicy dividend yield of 4.7%, 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 ever been in decades from an income standpoint. The stock's current P/E ratio of 16.7 is notably lower than its historical average. However, the company has limited earnings growth potential in the medium-term, and interest rate hikes ahead will increase the cost of equity. Accordingly, we have set our fair P/E at 16. In any case, due to achieving half a century of consecutive annual dividend increases, the high yield is more than likely to attract investor interest going forward. Thus, we don't expect a heavy multiple compression ahead.

Safety, Quality, Competitive Advantage, & Recession Resiliency

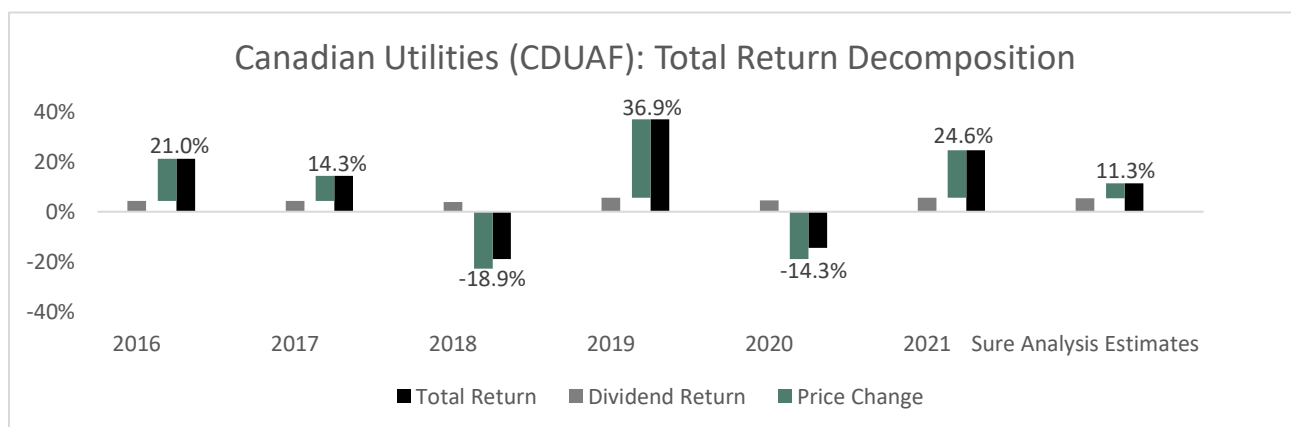
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	44%	46%	42%	105%	63%	86%	75%	52%	132%	81%	78%	73%

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 50 years, the company has withstood every one of them while raising its dividend. While Canadian Utilities' payout ratio were under pressure during 2020 (though dividends were in reality covered from its operating cash flows if we are to exclude depreciation and amortization,) by 2027 we expect it to have returned to much more comfortable levels, of around 73% 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 1.0% in local currency may suggest 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 high uncertainty. We project medium-term returns of around 11.3%, driven by the stock's high yield and modest EPS growth expectations. We rate the stock a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	\$3,040	\$3,283	\$3,261	\$2,557	\$2,567	\$3,152	\$3,378	\$2,942	\$2,413	2,804
Gross Profit	\$2,104	\$2,266	\$2,137	\$1,910	\$2,009	\$2,144	\$2,240	\$2,188	\$1,877	1,891
Gross Margin	69.2%	69.0%	65.5%	74.7%	78.3%	68.0%	66.3%	74.4%	77.8%	67.4%
SG&A Exp.	\$497	\$498	\$463	\$363	\$293	\$272	\$330	\$258	\$255	289
D&A Exp.	\$412	\$464	\$466	\$503	\$433	\$461	\$492	\$439	\$455	519
Operating Profit	\$943	\$1,033	\$922	\$639	\$898	\$917	\$835	\$963	\$702	696
Operating Margin	31.0%	31.5%	28.3%	25.0%	35.0%	29.1%	24.7%	32.7%	29.1%	24.8%
Net Profit	\$553	\$570	\$644	\$276	\$468	\$397	\$489	\$717	\$319	313
Net Margin	18.2%	17.4%	19.8%	10.8%	18.2%	12.6%	14.5%	24.4%	13.2%	11.2%
Free Cash Flow	-\$870	-\$517	-\$596	-\$43	\$248	\$73	-\$205	\$185	\$553	396
Income Tax	\$156	\$182	\$187	\$161	\$178	\$133	\$174	\$40	\$113	110

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	13,287	14,135	14,388	13,021	13,945	16,572	16,020	15,344	15,920	16,530
Cash & Equivalents	\$351	\$468	\$302	\$350	\$256	\$304	\$400	\$745	\$609	585
Accounts Receivable	\$533	\$448	\$418	\$312	\$384	\$469	\$496	\$389	\$426	507
Inventories	\$79	\$85	\$73	\$32	\$28	\$32	\$23	\$23	\$22	16
Goodwill & Int. Ass.	\$331	\$347	\$341	\$349	\$390	\$448	\$463	\$482	\$514	569
Total Liabilities	\$8,890	\$9,070	\$9,558	\$8,558	\$9,294	\$11,530	\$11,202	\$10,046	\$10,580	11,180
Long-Term Debt	\$5,502	\$5,910	\$6,305	\$5,759	\$6,214	\$7,890	\$7,694	\$6,864	\$7,102	7,464
Shareholder's Equity	\$3,670	\$4,019	\$3,870	\$3,259	\$3,401	\$3,714	\$3,592	\$4,020	\$4,029	3,972
LTD/E Ratio	1.25	1.17	1.31	1.33	1.38	1.61	1.64	1.33	1.37	1.43

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	4.5%	4.2%	4.5%	2.0%	3.5%	2.6%	3.0%	4.6%	2.0%	1.9%
Return on Equity	15.7%	14.8%	16.3%	7.7%	14.1%	11.1%	13.4%	18.8%	7.9%	7.8%
ROIC	6.0%	5.5%	5.8%	2.6%	4.4%	3.3%	3.8%	5.8%	2.6%	2.5%
Shares Out.	256.0	259.3	262.8	265.3	267.8	270.1	272.1	273.2	273	270
Revenue/Share	\$11.87	\$12.66	\$12.41	\$9.64	\$9.59	\$11.67	\$12.41	\$10.77	\$8.83	10.37
FCF/Share	-\$3.40	-\$1.99	-\$2.27	-\$0.16	\$0.93	\$0.27	-\$0.75	\$0.68	\$2.02	1.47

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

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