# NorthWestern Corp. (NWE)

*Updated May 12th, 2022, by Ian Bezek*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $59 | **5 Year CAGR Estimate:** | 7.0% | **Market Cap:** | $3.2 B |
| **Fair Value Price:** | $56 | **5 Year Growth Estimate:** | 4.5% | **Ex-Dividend Date:** | 06/14/22 |
| **% Fair Value:** | 105% | **5 Year Valuation Multiple Estimate:** | -1.0% | **Dividend Payment Date:** | 06/30/22 |
| **Dividend Yield:** | 4.3% | **5 Year Price Target** | $70 | **Years Of Dividend Growth:** | 17 |
| **Dividend Risk Score:** | C | **Retirement Suitability Score:** | B | **Rating:** | Hold |

## Overview & Current Events

NorthWestern Corp. is a Sioux Falls, South Dakota based electricity and gas utility. It has 1,500 employees, and primarily serves the states of South Dakota and Montana. The company's largest source of power generation is currently coal. However, it does produce 27% of its power from hydro and another 6% from wind. The company currently sources 35% of its electricity from power purchases rather than its own generation capacity. However, that will soon change as the company is building two new plants. One, a 58-megawatt plant in South Dakota, is scheduled to open in May 2022. Another larger 175-megawatt plant is supposed to come online in Montana in a few years, and the company has now begun site work for that facility.

On April 28th, 2022, NorthWestern announced its Q1 fiscal 2022 earnings. Operating revenues slipped 2% from the same period of 2021 to $394.5 million. The decline in revenues was partly due to a decrease in residential natural gas consumption in some of the company's markets. First quarter net income was $59.1 million, or $1.08 per diluted share, as compared with net income of $63.1 million, or $1.24 per diluted share, for the same period in 2021.

Despite the decline in top-line revenue, the company's gross margin rose $800,000 over the period. This is primarily due to the company spending less on fuel this quarter as opposed to the same quarter of 2021. The company's other expenses, such as depreciation, taxes, and operations and maintenance were largely unchanged from last year. The company maintained its previously stated earnings guidance for the remainder of 2022.

## Growth on a Per-Share Basis

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **EPS** | $2.26 | $2.46 | $2.99 | $2.90 | $3.39 | $3.34 | $3.40 | $3.53 | $3.06 | $3.60 | ***$3.28*** | ***$4.09*** |
| **DPS** | $1.48 | $1.52 | $1.60 | $1.92 | $2.00 | $2.10 | $2.20 | $2.30 | $2.40 | $2.48 | ***$2.52*** | ***$2.72*** |
| **Shares[1]** | 37.2 | 38.7 | 46.9 | 48.2 | 48.3 | 49.4 | 50.3 | 50.4 | 50.6 | 54.1 | ***58.0*** | ***63.0*** |

Since 2012, NorthWestern Corp. has grown its earnings per share by an average compounded rate of 5.3%. Meanwhile, it has grown its dividend by 5.9% per year on average over the same period. However, NorthWestern's growth has slowed significantly in recent years. The company's earnings have been roughly flat over the past five years through to 2022. The company's dividend hikes have also slowed down, with the latest increase being by just one cent per quarter.

Following a dip in earnings this year, we are forecasting 4.5% intermediate-term earnings growth, which falls in the middle part of management's range for longer-term earnings growth. The company is in a heavy investment cycle with its two new power facilities under way. 2022 will be the biggest capital investment year in NorthWestern's history. In light of that, it's understandable why NorthWestern has moved to smaller dividend increases than it has historically achieved. As part of that, the company has engaged in some dilution recently, which further limits the potential pace of earnings and dividend growth.

As the new power generation comes online, however, this should give a boost to Northwestern's earnings and allow it to return to more normal levels of growth.

[1] 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 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | Now | 2027 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Avg. P/E** | 15.7 | 16.9 | 16.2 | 18.4 | 17.2 | 17.8 | 16.8 | 19.9 | 19.5 | 16.9 | ***18.0*** | ***17.0*** |
| **Avg. Yld.** | 4.2% | 3.7% | 3.3% | 3.6% | 3.4% | 3.5% | 3.9% | 3.3% | 4.0% | 4.1% | ***4.3%*** | ***3.9%*** |

NorthWestern has historically had a stable P/E ratio with its average not going above 20 or below 15 over the past decade. Shares are currently well within their normal relative value range at 18.0 times earnings, though we see the company settling at 17 times earnings over the longer-term.

The company's dividend yield has generally run between the mid-3% to low 4% range. The current 4.3% dividend yield is a higher than usual entry point for NorthWestern stock. Offsetting the starting higher dividend yield, however, is the fact that dividend growth has significantly decelerated over the past couple of years. And dividend growth may remain muted until the company's current capital investment cycle concludes.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Payout** | 65% | 62% | 54% | 66% | 59% | 63% | 65% | 65% | 78% | 69% | ***77%*** | ***67%*** |

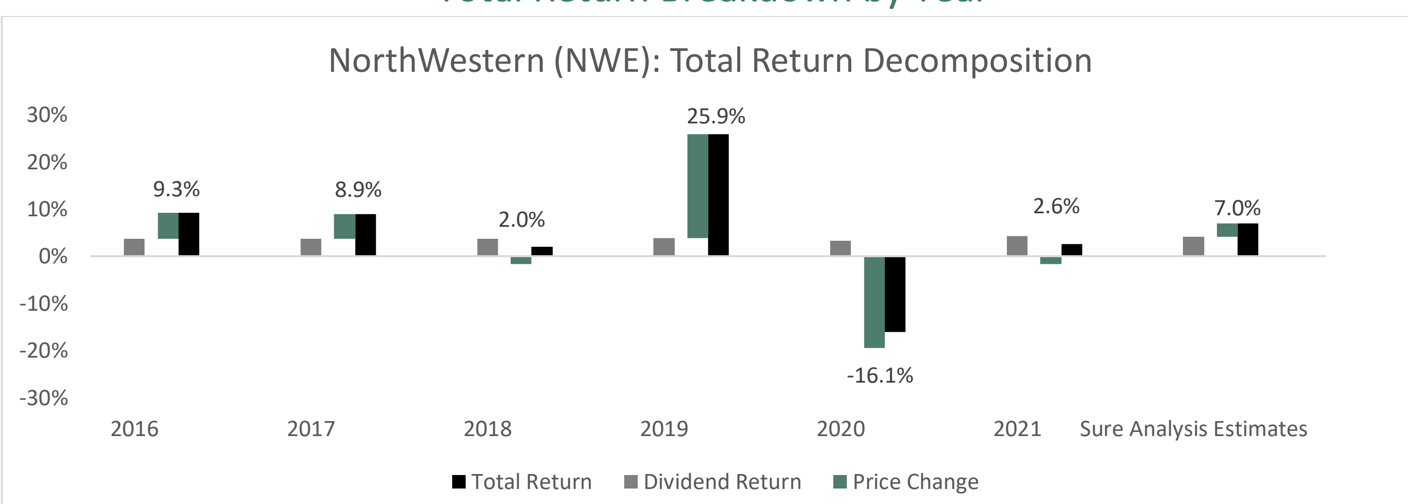
NorthWestern is somewhat on the small side as far as publicly traded utilities go and could face some geographical risk if anything happens to curb power demand in key states such as South Dakota and Montana. However, utilities, as an industry, are highly resilient and tend to fare relatively well during economic duress.

NorthWestern aims to have its dividend payout ratio be between 60% and 70%. However, it has now crept up to 77% based on this year's projected earnings. We project that earnings will grow more quickly than dividends through 2027 as NorthWestern seeks to get its payout ratio back down to something below 70%.

## Final Thoughts & Recommendation

NorthWestern shares have fallen 9% over the past year, making for a relatively more attractive entry point. We now estimate 7.0% per year total return potential, driven by a 4.5% earnings growth rate and the starting dividend yield along with a small drag from a decrease in its valuation. There is some execution risk around the company's new power plants, and dividend hikes will likely be somewhat subdued versus past growth. However, the starting 4.3% dividend yield helps counterbalance those points. Shares earn a hold rating.

## Total Return Breakdown by Year

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## Income Statement Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 1,070 | 1,155 | 1,205 | 1,214 | 1,257 | 1,306 | 1,192 | 1,258 | 1,199 | 1,372 |
| Gross Profit | 675 | 675 | 722 | 841 | 856 | 895 | 919 | 940 | 892 | 947 |
| Gross Margin | 63.1% | 58.5% | 59.9% | 69.3% | 68.1% | 68.6% | 77.1% | 74.7% | 74.5% | 69.0% |
| SG&A Exp. | 270 | 286 | 306 | 297 | 294 | 295 | 307 | 109 | 94 | 102 |
| Operating Profit | 201 | 171 | 178 | 266 | 255 | 272 | 266 | 277 | 236 | 276 |
| Operating Margin | 18.8% | 14.8% | 14.8% | 21.9% | 20.3% | 20.8% | 22.3% | 22.0% | 19.7% | 20.1% |
| Net Profit | 98 | 94 | 121 | 151 | 164 | 163 | 197 | 202 | 155 | 187 |
| Net Margin | 9.2% | 8.1% | 10.0% | 12.5% | 13.1% | 12.5% | 16.5% | 16.1% | 12.9% | 13.6% |
| Free Cash Flow | 32 | (37) | (20) | 56 | (1) | 46 | 98 | (19) | (54) | (214) |
| Income Tax | 18 | 14 | (10) | 30 | (8) | 13 | (19) | (20) | (11) | 3 |

## Balance Sheet Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|---|---|
| Total Assets | 3,486 | 3,715 | 4,974 | 5,265 | 5,499 | 5,421 | 5,644 | 6,083 | 6,389 | 6,780 |
| Cash & Equivalents | 10 | 17 | 20 | 12 | 5 | 8 | 8 | 5 | 6 | 3 |
| Acc. Receivable | 144 | 175 | 163 | 154 | 160 | 182 | 162 | 167 | 168 | 199 |
| Inventories | 54 | 56 | 55 | 53 | 49 | 52 | 51 | 54 | 61 | 81 |
| Total Liabilities | 355 | 355 | 355 | 358 | 358 | 358 | 358 | 358 | 358 | 358 |
| Accounts Payable | 2,552 | 2,685 | 3,496 | 3,665 | 3,823 | 3,622 | 3,702 | 4,044 | 4,310 | 4,441 |
| Long-Term Debt | 84 | 93 | 82 | 75 | 79 | 85 | 87 | 97 | 100 | 115 |
| Total Equity | 1,178 | 1,296 | 1,930 | 1,998 | 2,094 | 2,113 | 2,102 | 2,233 | 2,415 | 2,541 |
| LTD/E Ratio | 934 | 1,031 | 1,478 | 1,600 | 1,676 | 1,799 | 1,942 | 2,039 | 2,079 | 2,340 |

## Profitability & Per Share Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|---|---|
| Return on Assets | 2.9% | 2.6% | 2.8% | 3.0% | 3.1% | 3.0% | 3.6% | 3.4% | 2.5% | 2.8% |
| Return on Equity | 11.0% | 9.6% | 9.6% | 9.8% | 10.0% | 9.4% | 10.5% | 10.2% | 7.5% | 8.5% |
| ROIC | 4.9% | 4.2% | 4.2% | 4.3% | 4.5% | 4.2% | 5.0% | 4.9% | 3.5% | 4.0% |
| Shares Out. | 37.2 | 38.7 | 46.9 | 48.2 | 48.3 | 49.4 | 50.3 | 50.4 | 50.6 | 54.1 |
| Revenue/Share | 28.93 | 30.27 | 29.85 | 25.46 | 25.94 | 26.83 | 23.73 | 24.94 | 23.71 | 26.54 |
| FCF/Share | 0.86 | (0.96) | (0.50) | 1.18 | (0.02) | 0.95 | 1.95 | (0.38) | (1.06) | (4.15) |

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