



# Canadian Utilities (CDUAF)

Updated July 28<sup>th</sup>, 2022 by Nikolaos Sismanis

## Key Metrics

<b>Current Price:</b>	\$32	<b>5 Year CAGR Estimate:</b>	11.6%	<b>Market Cap:</b>	\$8.71 B
<b>Fair Value Price:</b>	\$29	<b>5 Year Growth Estimate:</b>	4.0%	<b>Ex-Dividend Date:</b>	08/03/2022
<b>% Fair Value:</b>	112%	<b>5 Year Valuation Multiple Estimate:</b>	-2.2%	<b>Dividend Payment Date:</b>	09/01/2022
<b>Dividend Yield:</b>	4.3%	<b>5 Year Price Target</b>	\$35	<b>Years Of Dividend Growth<sup>1</sup>:</b>	50
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	A	<b>Rating</b>	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 dollars are used in this research report.

On July 28<sup>th</sup>, 2022, Canadian Utilities reported its Q2-2022 results for the period ending June 30<sup>th</sup>, 2022. Revenues for the quarter amounted to \$726, 18.1% higher year-over-year, while EPS came in at \$0.39 compared to a loss of \$0.03 in Q2-2022.

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 inflation indexing on the rate base in Australia, the impact of the 2018-2019 General Tariff Application Compliance Filing decision, and the timing of operating costs in the Natural Gas Distribution business.

Our updated estimates point towards FY2022 EPS of \$1.80 (previously \$1.77). The company's current annualized dividend rate of C\$1.7768 equals close to US\$1.37 at the current FX rates.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>EPS</b>	\$2.04	\$1.97	\$2.18	\$0.81	\$1.54	\$1.32	\$1.53	\$2.50	\$1.04	\$1.69	<b>\$1.80</b>	<b>\$2.19</b>
<b>DPS</b>	\$0.89	\$0.91	\$0.92	\$0.85	\$0.97	\$1.14	\$1.15	\$1.30	\$1.37	\$1.37	<b>\$1.37</b>	<b>\$1.55</b>
<b>Shares<sup>2</sup></b>	255	255	258	262	265	267	269	272	272	270	<b>269</b>	<b>350</b>

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.

<sup>1</sup> Years of Dividend Growth and Last Dividend Increase based in C\$.

<sup>2</sup> 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	17.9	16.0
Avg. Yld.	2.7%	2.7%	2.7%	3.4%	3.6%	3.5%	4.6%	4.8%	4.8%	4.8%	4.3%	4.4%

Canadian Utilities' shares are currently attached to a high dividend yield of 4.3%, offering attractive tangible returns in the form of quarterly income. The yield is also currently above the company's 10-year average, which makes this legendary dividend payer even more attractive from an income standpoint. The stock's current P/E ratio of 17.9 is close to its historical average. However, the company has limited earnings growth potential in the medium-term, and interest rate hikes should 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

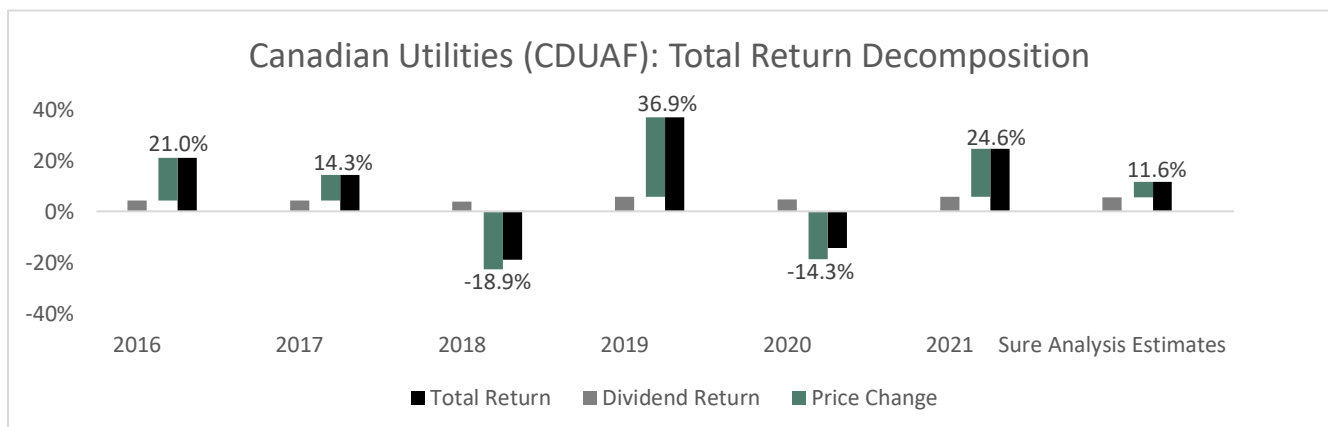
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	44%	46%	42%	105%	63%	86%	75%	52%	132%	81%	76%	71%

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 71% 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 still remains quite 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 11.6%, driven by the stock's dividend yield and modest EPS growth expectations, offset by modest valuation headwinds. We continue to 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
<b>Revenue</b>	\$3,040	\$3,283	\$3,261	\$2,557	\$2,567	\$3,152	\$3,378	\$2,942	\$2,413	2,804
<b>Gross Profit</b>	\$2,104	\$2,266	\$2,137	\$1,910	\$2,009	\$2,144	\$2,240	\$2,188	\$1,877	1,891
<b>Gross Margin</b>	69.2%	69.0%	65.5%	74.7%	78.3%	68.0%	66.3%	74.4%	77.8%	67.4%
<b>SG&amp;A Exp.</b>	\$497	\$498	\$463	\$363	\$293	\$272	\$330	\$258	\$255	289
<b>D&amp;A Exp.</b>	\$412	\$464	\$466	\$503	\$433	\$461	\$492	\$439	\$455	519
<b>Operating Profit</b>	\$943	\$1,033	\$922	\$639	\$898	\$917	\$835	\$963	\$702	696
<b>Operating Margin</b>	31.0%	31.5%	28.3%	25.0%	35.0%	29.1%	24.7%	32.7%	29.1%	24.8%
<b>Net Profit</b>	\$553	\$570	\$644	\$276	\$468	\$397	\$489	\$717	\$319	313
<b>Net Margin</b>	18.2%	17.4%	19.8%	10.8%	18.2%	12.6%	14.5%	24.4%	13.2%	11.2%
<b>Free Cash Flow</b>	-\$870	-\$517	-\$596	-\$43	\$248	\$73	-\$205	\$185	\$553	396
<b>Income Tax</b>	\$156	\$182	\$187	\$161	\$178	\$133	\$174	\$40	\$113	110

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Total Assets</b>	13,287	14,135	14,388	13,021	13,945	16,572	16,020	15,344	15,920	16,530
<b>Cash &amp; Equivalents</b>	\$351	\$468	\$302	\$350	\$256	\$304	\$400	\$745	\$609	585
<b>Accounts Receivable</b>	\$533	\$448	\$418	\$312	\$384	\$469	\$496	\$389	\$426	507
<b>Inventories</b>	\$79	\$85	\$73	\$32	\$28	\$32	\$23	\$23	\$22	16
<b>Goodwill &amp; Int. Ass.</b>	\$331	\$347	\$341	\$349	\$390	\$448	\$463	\$482	\$514	569
<b>Total Liabilities</b>	\$8,890	\$9,070	\$9,558	\$8,558	\$9,294	\$11,530	\$11,202	\$10,046	\$10,580	11,180
<b>Long-Term Debt</b>	\$5,502	\$5,910	\$6,305	\$5,759	\$6,214	\$7,890	\$7,694	\$6,864	\$7,102	7,464
<b>Shareholder's Equity</b>	\$3,670	\$4,019	\$3,870	\$3,259	\$3,401	\$3,714	\$3,592	\$4,020	\$4,029	3,972
<b>LTD/E Ratio</b>	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
<b>Return on Assets</b>	4.5%	4.2%	4.5%	2.0%	3.5%	2.6%	3.0%	4.6%	2.0%	1.9%
<b>Return on Equity</b>	15.7%	14.8%	16.3%	7.7%	14.1%	11.1%	13.4%	18.8%	7.9%	7.8%
<b>ROIC</b>	6.0%	5.5%	5.8%	2.6%	4.4%	3.3%	3.8%	5.8%	2.6%	2.5%
<b>Shares Out.</b>	256.0	259.3	262.8	265.3	267.8	270.1	272.1	273.2	273	270
<b>Revenue/Share</b>	\$11.87	\$12.66	\$12.41	\$9.64	\$9.59	\$11.67	\$12.41	\$10.77	\$8.83	10.37
<b>FCF/Share</b>	-\$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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