Stantec Inc. (STN)

Updated February 28th, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	$58	**5 Year CAGR Estimate:**	9.1%	**Market Cap:**	$6.5 B
Fair Value Price:	$52	**5 Year Growth Estimate:**	11.0%	**Ex-Dividend Date:**	03/30/2023
% Fair Value:	113%	**5 Year Valuation Multiple Estimate:**	-2.5%	**Dividend Payment Date:**	04/17/2023
Dividend Yield:	1.0%	**5 Year Price Target**	$87	**Years Of Dividend Growth:**	11[1]
Dividend Risk Score:	C	**Retirement Suitability Score:**	F	**Rating:**	Hold

Overview & Current Events

Stantec Inc. provides professional consulting services in the field of infrastructure and facilities internationally. This includes services in engineering, architecture, interior design, environmental sciences, project management, and project economics. The company also undertakes water provision, transportation, and public works such as transportation planning and traffic engineering. Finally, it serves the urban regeneration, infrastructure, education, and waste industries. Stantec generated $3.3 billion in revenues last year and is based in Edmonton, Canada. All figures in this report have been converted to U.S. dollars.

On February 22nd, 2023, Stantec released its Q4-2022 and full-year results for the period ending December 31st, 2022. Quarterly net revenues came in at $834.9 million, 23.4% higher on a constant basis year-over-year, reflecting 10.6% organic and 9.8% acquisition net revenue growth. Adjusted net income increased by 42.8% to $20.0 million. While the project margin fell from 55.3% to 54.9%, administrative and marketing expenses as a percentage of net sales declined from 42.3% to 39.9% - hence the increase.

On a per-share basis, adjusted net income was $0.82, implying a year-over-year growth of 43.9%, as it was further boosted by a lower share count. The company's contract backlog increased to $4.3 billion, 14.9% higher year-over-year, including double-digit growth in Buildings and Energy & Resources and Environmental Services backlog. It represents about 12 months' of work.

For the full year, management expects net revenue growth between 7% and 11% and adjusted EPS growth between 9% and 13% in comparison to FY2022. Accordingly, we estimate FY2023 adjusted EPS of $2.58, which is derived from: FY2022 adjusted EPS of CAD3.13 times 1.115 (midpoint of guidance) times 0.74 (CAD/USD). Note that all figures in the table below reflect GAAP EPS. We are utilizing adjusted EPS in estimating the company's total return prospects. Finally, along with its earnings report, the company increased its dividend by 8.3% to a quarterly rate of CAD0.195. At the current exchange rate, it implies an annualized dividend of $0.57 in USD.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$1.49	$1.52	$1.20	$0.91	$0.68	$0.31	$1.34	$1.21	$1.43	$1.64	***$2.58***	***$4.35***
DPS	$0.31	$0.32	$0.30	$0.34	$0.40	$0.40	$0.45	$0.49	$0.52	$0.53	***$0.57***	***$0.76***
Shares[2]	92.5	93.5	94.1	107	114	113.7	111.6	111.6	111.2	110.9	***110.9***	***105.0***

Stantec has been growing its revenues consistently over the past two decades, riding the wave of increased spending in infrastructure, net zero-designed buildings, and green energy. EPS lagged from 2013 to 2019, as the company took advantage of its increased operating cash flows to acquire other companies and reinvest back into its business. With scaling, EPS has also started to accelerate over the past few years, and it should continue to do so as the company's margins undergo an expansion phase. We expect an EPS medium-term growth of 11%, powered by the global trend of increased spending in green energy, smart cities, ecosystem restorations, and clean infrastructure. The company has

[1] Based on the original Canadian listing.
[2] Share count is 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.

grown its dividend annually in its original CAD reporting since initiating one in 2012. However, in its NYSE listing, dividend growth has lagged due to the Canadian dollar's prolonged depreciation against the USD. This applies to the company's EPS performance as well. We expect DPS growth of around 6% in the medium-term, lower than Stantec's latest DPS hike, assuming the company retains sufficient cash to reinvest towards its future prosperity.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	16.1	21.7	29.2	35.2	50.9	103.2	23.1	32.2	33.5	28.7	***22.7***	***20.0***
Avg. Yld.	1.3%	1.0%	0.9%	1.1%	1.2%	1.3%	1.5%	1.3%	1.0%	1.1%	***1.0%***	***0.9%***

Stantec's P/E ratio has fluctuated wildly over the past decade due to volatile EPS for the reasons mentioned earlier. However, note that all historical P/E figures relate to the company's GAAP metrics, which are usually affected by extraordinary events. The stock's current valuation of 22.7 times the expected FY2023 adjusted EPS could modestly overvalue the stock. We are aware of Stantec's robust backlog, which should keep producing resilient results, but we remain mindful of global spending potential slowing down in the near future. Investors should expect a tiny yield in the coming years, as the company retains most of its free cash flow towards funding its future project delivery capabilities.

Safety, Quality, Competitive Advantage, & Recession Resiliency

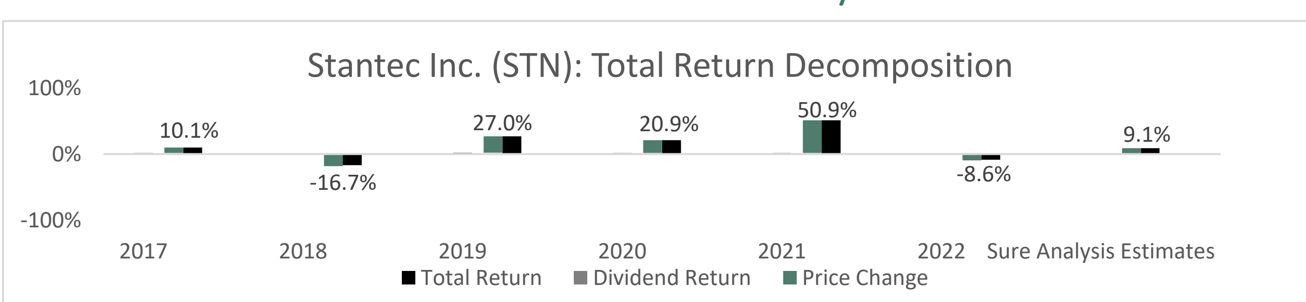
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	21%	21%	25%	37%	59%	129%	34%	40%	36%	32%	***22%***	***18%***

We consider Stantec's dividend very safe. Not only is the payout ratio quite healthy, but EPS is growing at a faster rate than DPS. Further, the company reports high depreciation and amortization levels. Hence, the dividend is covered by an even wider margin from cash from operations. Additionally, Stantec showcases great operational qualities, such as its year-long worth of revenues of backlog, which should be able to sustain a stable performance if demand for its services faces temporary headwinds. We can't identify and particular competitive advantages, though the company's massively wide array of services could make it a more desirable option for future clients against its competitors, which operate in smaller, fragmented markets. Due to having a strong backlog and due to infrastructure and water revenues being secured under long-term contracts, we believe that financials will remain resilient under a potential recession, as was the case during the Great Financials Crisis. Financials remained excellent during the COVID-19 pandemic as well.

Final Thoughts & Recommendation

Stantec exhibits an extended record of excellent shareholder value creation. The company is operating in an industry full of favorable growth catalysts ahead, which should result in higher financials and a solid backlog going forward. We forecast annualized returns of 9.1% in the medium-term. Accordingly, Stantec earns a hold rating. American investors should be wary of the FX fluctuations between the USD and CAD, which could sway returns either way.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	1,871	2,172	2,292	2,254	3,247	3,109	3,306	3,637	3,530	3,651
Gross Profit	854	974	1,031	1,013	1,266	1,359	1,401	1,513	1,441	1,566
Gross Margin	45.7%	44.8%	45.0%	44.9%	39.0%	43.7%	42.4%	41.6%	40.8%	42.9%
SG&A Exp.	632	725	766	775	1,008	1,086	1,110	1,080	1,010	1,135
D&A Exp.	48	52	57	66	96	---	---	---	---	177
Operating Profit	174	197	208	173	162	177	202	252	260	254
Operating Margin	9.3%	9.1%	9.1%	7.7%	5.0%	5.7%	6.1%	6.9%	7.4%	7.0%
Net Profit	121	142	149	123	99	75	37	146	128	160
Net Margin	6.5%	6.5%	6.5%	5.4%	3.0%	2.4%	1.1%	4.0%	3.6%	4.4%
Free Cash Flow	149	209	146	128	166	154	---	---	---	276
Income Tax	43	51	53	43	38	128	42	54	43	50

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	1,472	1,567	1,688	1,688	3,178	3,088	2,944	3,492	3,442	4,099
Cash & Equivalents	41	134	132	49	156	190	130	171	224	152
Accounts Receivable	350	353	362	403	549	594	569	603	551	618
Goodwill & Int. Ass.	656	633	739	796	1,689	1,447	1,372	1,433	1,455	2,006
Total Liabilities	741	728	752	734	1,712	1,578	1,543	2,055	1,929	2,529
Accounts Payable	64	80	90	89	270	292	163	173	171	167
Long-Term Debt	301	224	266	263	757	588	686	674	538	982
Shareholder's Equity	731	838	936	954	1,465	1,508	1,400	1,436	1,512	1,570
LTD/E Ratio	0.41	0.27	0.28	0.28	0.52	0.39	0.49	0.47	0.36	0.63

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	8.7%	9.3%	9.2%	7.3%	4.1%	2.4%	1.2%	4.6%	3.7%	4.3%
Return on Equity	18.0%	18.1%	16.8%	13.0%	8.1%	5.0%	2.5%	10.3%	8.7%	10.4%
ROIC	12.5%	13.6%	13.2%	10.1%	5.7%	3.5%	1.7%	7.0%	6.1%	7.0%
Shares Out.	91.5	92.5	93.5	94.1	107	114	113.7	111.6	111.6	111.6
Revenue/Share	20.42	23.31	24.29	23.83	30.25	27.18	29.04	32.61	31.54	32.71
FCF/Share	1.63	2.24	1.55	1.36	1.55	1.35	---	---	---	2.48

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