



Fortis Inc. (FTS)

Updated May 9th, 2023 by Kay Ng

Key Metrics

Current Price:	\$46	5 Year CAGR Estimate:	8.3%	Market Cap:	\$22B
Fair Value Price:	\$44	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	05/16/23
% Fair Value:	105%	5 Year Valuation Multiple Estimate:	-1.0%	Dividend Payment Date:	06/01/23
Dividend Yield:	3.7%	5 Year Price Target	\$58	Years Of Dividend Growth:	49
Dividend Risk Score:	B	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

Fortis is Canada's largest investor-owned utility business with operations in Canada, the United States, and the Caribbean. It is cross-listed in Toronto and New York. Fortis trades with a current after-tax yield of 3.1% (about 3.7% before the 15% withholding tax applied by the Canadian government). Unless otherwise noted, US\$ is used in this research report. At the end of 2022, Fortis had 99% regulated assets: 82% regulated electric and 17% regulated gas. As well, 64% were in the U.S., 33% in Canada, and 3% in the Caribbean.

Fortis reported Q1 2023 results on 05/03/23. For the quarter, it reported adjusted net earnings of C\$437 million, up 25% versus Q1 2022, while adjusted earnings-per-share (EPS) rose 17% to C\$0.91. The company noted that the increase reflected rate base growth, mainly at ITC and the western Canadian utilities, and higher earnings at UNS Energy. The company's capital investments in the quarter were C\$1.0 billion, and it's on track to make C\$4.3 billion of capital investments this year. We maintain our 2023 EPS estimate at \$2.20.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$1.60	\$1.56	\$1.52	\$1.78	\$2.02	\$1.89	\$1.92	\$2.02	\$2.04	\$2.08	\$2.20	\$2.94
DPS	\$1.20	\$1.16	\$1.09	\$1.15	\$1.25	\$1.33	\$1.38	\$1.44	\$1.64	\$1.67	\$1.69	\$2.16
Shares¹	213	276	282	401	421	429	447	465	471	479	485	518

Fortis compounded its EPS at 5.6% and DPS at 6.4% per year from 2013 to 2022 in C\$. After releasing its five-year capital plan of C\$22.3 billion for 2023 to 2027, which suggests a mid-year rate base growth at a compound annual growth rate of ~6.2% from C\$34.1 billion in 2022 to C\$46.1 billion in 2027, the company also revealed its dividend growth guidance of 4-6% through 2027. We extend those growth rates for EPS and DPS of 6% and 5%, respectively, from 2023 to 2028.

The capital plan includes investing in areas, such as a greener and improved grid and a shift from fossil fuel to solar and wind generation. Importantly, this growth rate is *before* the impact of acquisitions, which have historically been important for Fortis. Notably, the picture doesn't look as rosy from a US\$ perspective. In US\$, Fortis compounded its EPS and DPS, respectively, at only 3.0% and 3.7% per year from 2013 to 2022.

Additionally, the utility tends to use equity offerings as a source of capital to pay down debt or make acquisitions, resulting in a greater number of common shares. Our estimates account for a steady rise in the share count, but just how many shares are issued depends on Fortis' future acquisitions. This is a variable in the outlook that can impact results, particularly if Fortis completes a sizable acquisition funded by stock.

The company will continue to grow steadily as the regulated utility aims to reduce 50% of carbon emissions by 2030 and 75% by 2035 compared to 2019. A key part of the plan is to exit all coal-fired generation by 2032.

¹ Shares 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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	16.9	18.2	17.8	28.1	40.6	21.2	19.9	20.0	21.7	21.7	20.8	19.8
Avg. Yld.	4.1%	3.7%	3.3%	3.1%	3.1%	2.9%	3.1%	3.5%	3.5%	3.6%	3.7%	3.7%

Fortis stock averaged a P/E of 22.6 from 2013-2022, but the average multiple drops to 20.6 when the 2017 outlier is taken out. So, we target a fair target P/E of 19.8. Using our 2023 EPS estimate, Fortis trades at a price-to-earnings ratio of 20.8, which makes it a fairly-valued stock. Fortis is currently trading with a dividend yield of 3.7% (gross of the withholding tax paid to the Canadian government). This is safe income generation from a blue-chip North American utility.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	75%	74%	72%	65%	62%	70%	72%	71%	80%	80%	77%	73%

Because demand for Fortis's utility services doesn't change much in various economic environments, Fortis's results have been quite resilient through economic uncertainties, including the one we're experiencing in which inflation and interest rates are higher than recent history.

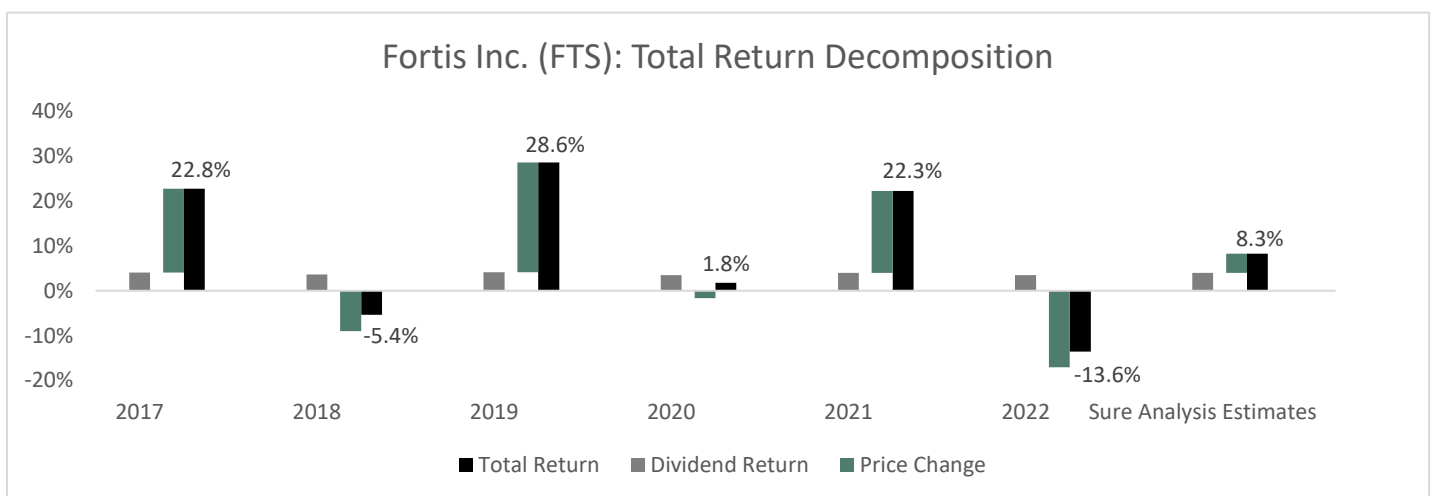
Fortis's liquidity position is strong, including C\$3.6 billion of undrawn liquidity available from \$5.8-billion credit facilities at the end of Q1 2023. Fortis' payout ratio had been about 70% of earnings, which is where it's heading. The dividend is important to management and we believe it is safe and should continue to rise for years to come.

Fortis' competitive advantage is its size and scale. In addition, Fortis is unique because of its cross-border exposure. Its timely U.S. acquisitions of regulated utilities since 2013 have allowed Fortis to now generate more than half of its revenue from the country.

Final Thoughts & Recommendation

Fortis is a quality North American regulated utility that has a leading position. We estimate FTS will deliver a total rate of return of 8.3% through 2028 from 6% earnings growth, a 3.7% yield, and a P/E compression of 1.0%. We rate FTS stock as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	3,930	4,892	5,294	5,164	6,405	6,474	6,618	6,669	7,536	8,488
Gross Profit	2,360	2,902	3,264	3,396	4,583	4,549	4,719	4,757	5,182	5,450
Gross Margin	60.0%	59.3%	61.7%	65.8%	71.6%	70.3%	71.3%	71.3%	68.8%	64.2%
D&A Exp.	525	623	684	742	910	959	1,017	1,066	1,200	1,282
Operating Profit	827	927	1,112	1,120	1,938	1,825	1,854	1,872	1,969	2,106
Operating Margin	21.1%	18.9%	21.0%	21.7%	30.2%	28.2%	28.0%	28.1%	26.1%	24.8%
Net Profit	398	343	631	498	793	900	1,297	951	1,032	1,071
Net Margin	10.1%	7.0%	11.9%	9.7%	12.4%	13.9%	19.6%	14.3%	13.7%	12.6%
Free Cash Flow	-268	-673	-447	-134	-207	-474	-796	-999	-382	-608
Income Tax	31	60	175	109	454	127	218	172	187	222

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	16,819	22,598	20,757	35,530	38,029	38,950	40,883	43,509	45,222	47,342
Cash & Equivalents	68	198	174	200	260	244	283	195	103	154
Accounts Receivable	331	413	373	376	366	395	386	467	487	685
Inventories	134	277	243	276	292	292	302	331	375	487
Goodwill & Int. Ass.	2,273	3612	3,397	9,920	10,119	10,081	10,154	10,260	10,245	10,324
Total Liabilities	10,831	14,749	13,296	23,329	24,710	25,400	25,486	27,602	28,818	30,511
Accounts Payable	397	527	298	411	553	499	577	554	607	653
Long-Term Debt	6,963	9,320	8,456	16,527	17,231	17,727	17,380	19,212	20,064	21,121
Shareholder's Equity	4,482	5,919	5,808	9,623	10,640	10,947	12,944	13,390	13,855	14,299
LTD/E Ratio	1.24	1.24	1.19	1.53	1.44	1.46	1.23	1.31	1.33	1.36

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	2.5%	1.7%	2.9%	1.8%	2.2%	2.3%	3.3%	2.3%	2.3%	2.3%
Return on Equity	9.4%	6.6%	10.8%	6.5%	7.8%	8.3%	10.9%	7.2%	7.6%	7.6%
ROIC	3.2%	2.3%	3.8%	2.2%	2.7%	2.9%	4.1%	2.8%	2.9%	2.9%
Shares Out.	213	276	282	401	421	429	447	465	471	479
Revenue/Share	18.78	21.64	18.60	16.48	15.39	15.23	15.13	14.33	15.99	17.72
FCF/Share	-1.28	-2.98	-1.57	-0.43	-0.50	-1.11	-1.82	-2.15	-0.81	-1.27

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

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