Stantec Inc. (STN)

Updated August 13th, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	$67	**5 Year CAGR Estimate:**	6.7%	**Market Cap:**	$7.4 B
Fair Value Price:	$53	**5 Year Growth Estimate:**	11.0%	**Ex-Dividend Date:**	09/28/2023
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.6%	**Dividend Payment Date:**	10/16/2023
Dividend Yield:	0.9%	**5 Year Price Target**	$89	**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 August 10th, 2023, Stantec released its Q2 results for the period ending June 30th, 2023. Quarterly net revenues came in at $965.3 million, 14.5% higher on a constant basis year-over-year, reflecting 11.2% organic and 3.3% acquisition net revenue growth. Adjusted net income increased by 18.1% to nearly $81.4 million. This was due to Stantec's project margin rising from 54.0% to 54.3%, and administrative and marketing expenses as a percentage of net sales declining from 39.1% to 38.6%.

On a per-share basis, adjusted net income was $0.74, implying year-over-year growth of 19.3%, as it was further boosted by a lower share count. The company's contract backlog increased to $4.9 billion, a record high reflecting 10.0% organic growth year-to-date, including double-digit growth in Environmental Services and Water backlog. It represents about 13 months of work.

For the full year, management expects net revenue growth between 10% and 13% and adjusted EPS growth between 12% and 15% in comparison to FY2022. Accordingly, we estimate FY2023 adjusted EPS of $2.63, which is derived from: FY2022 adjusted EPS of CAD3.13 times 1.135 (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, the quarterly dividend rate of C$0.195 implies an annualized dividend of $0.58 in USD at the current exchange rate.

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	***$2.63***	***$4.43***
DPS	$0.31	$0.32	$0.30	$0.34	$0.40	$0.40	$0.45	$0.49	$0.52	$0.53	***$0.58***	***$0.78***
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 grown its dividend annually in its original CAD reporting since initiating one in 2012. However, in its NYSE listing,

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

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	***25.4***	***20.0***
Avg. Yld.	1.3%	1.0%	0.9%	1.1%	1.2%	1.3%	1.5%	1.3%	1.0%	1.1%	***0.9%***	***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 25.4 times the expected FY2023 adjusted EPS could overvalue the name. 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 and rising interest rates. Investors should expect a low yield in the coming years, as Stantec retains most of its free cash flow towards funding its future project delivery capabilities.

Safety, Quality, Competitive Advantage, & Recession Resiliency

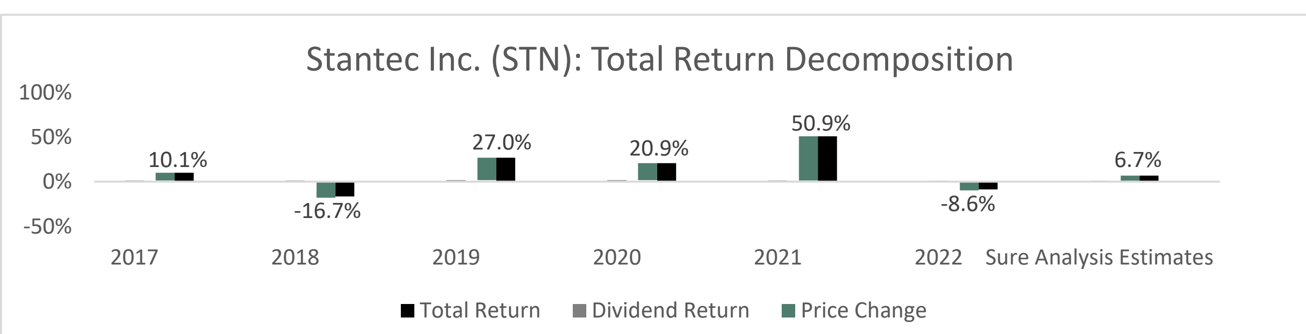
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	21%	21%	25%	37%	59%	129%	34%	40%	36%	32%	***22%***	***18%***

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 with favorable growth catalysts ahead, which should result in higher financials and a solid backlog going forward. We forecast annualized returns of 6.7% 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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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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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	2,172	2,292	2,254	3,247	3,109	3,306	3,637	3,530	3,651	4,364
Gross Profit	974	1,031	1,013	1,266	1,359	1,401	1,513	1,441	1,566	1,858
Gross Margin	44.8%	45.0%	44.9%	39.0%	43.7%	42.4%	41.6%	40.8%	42.9%	42.6%
SG&A Exp.	725	766	775	1,008	1,086	1,110	1,080	1,010	1,135	1,339
D&A Exp.	52	57	66	96	---	---	---	---	177	218
Operating Profit	197	208	173	162	177	202	252	260	254	301
Operating Margin	9.1%	9.1%	7.7%	5.0%	5.7%	6.1%	6.9%	7.4%	7.0%	6.9%
Net Profit	142	149	123	99	75	37	146	128	160	190
Net Margin	6.5%	6.5%	5.4%	3.0%	2.4%	1.1%	4.0%	3.6%	4.4%	4.4%
Free Cash Flow	209	146	128	166	154	---	---	---	276	176
Income Tax	51	53	43	38	128	42	54	43	50	60

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,567	1,688	1,688	3,178	3,088	2,944	3,492	3,442	4,099	4,165
Cash & Equivalents	134	132	49	156	190	130	171	224	152	109
Accounts Receivable	353	362	403	549	594	569	603	551	618	728
Goodwill & Int. Ass.	633	739	796	1,689	1,447	1,372	1,433	1,455	2,006	1,965
Total Liabilities	728	752	734	1,712	1,578	1,543	2,055	1,929	2,529	2,480
Accounts Payable	80	90	89	270	292	163	173	171	167	221
Long-Term Debt	224	266	263	757	588	686	674	538	982	959
Shareholder's Equity	838	936	954	1,465	1,508	1,400	1,436	1,512	1,570	1,684
LTD/E Ratio	0.27	0.28	0.28	0.52	0.39	0.49	0.47	0.36	0.63	0.57

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	9.3%	9.2%	7.3%	4.1%	2.4%	1.2%	4.6%	3.7%	4.3%	4.6%
Return on Equity	18.1%	16.8%	13.0%	8.1%	5.0%	2.5%	10.3%	8.7%	10.4%	11.7%
ROIC	13.6%	13.2%	10.1%	5.7%	3.5%	1.7%	7.0%	6.1%	7.0%	7.3%
Shares Out.	92.5	93.5	94.1	107	114	113.7	111.6	111.6	111.6	111.1
Revenue/Share	23.31	24.29	23.83	30.25	27.18	29.04	32.61	31.54	32.71	39.29
FCF/Share	2.24	1.55	1.36	1.55	1.35	---	---	---	2.48	1.59

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