



# Algonquin Power & Utilities Corp. (AQN)

Updated September 8<sup>th</sup>, 2023 by Kay Ng

## Key Metrics

<b>Current Price:</b>	\$7	<b>5 Year CAGR Estimate:</b>	11.0%	<b>Market Cap:</b>	\$4.9B
<b>Fair Value Price:</b>	\$8	<b>5 Year Growth Estimate:</b>	4.0%	<b>Ex-Dividend Date:</b>	09/27/23
<b>% Fair Value:</b>	91%	<b>5 Year Valuation Multiple Estimate:</b>	2.0%	<b>Dividend Payment Date:</b>	10/13/23
<b>Dividend Yield:</b>	6.1%	<b>5 Year Price Target</b>	\$10	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	D	<b>Rating:</b>	Hold

## Overview & Current Events

Algonquin Power & Utilities Corp. trades on both the Toronto Stock Exchange and New York Stock Exchange under the ticker, AQN. The renewable power and utility company was founded in 1988. All the figures in this report are in U.S. dollars unless otherwise noted.

Alongside its Q2 2023 results reported on 8/10/23, Algonquin had a big announcement with the intention to sell its renewable energy business, which will make the company a pure-play regulated utility. As well, Christopher Huskilson, an Algonquin Board member, was appointed interim CEO. Its regulated utilities are diversified across natural gas, electric, and water. It anticipates to use the proceeds from the sale of the renewable portfolio for debt reduction and share repurchases. The sale would also help support its current dividend, reduce its cost of capital, and maintain its investment-grade credit rating of BBB. The successful sale of the renewable portfolio should help the utility stock trade closer to the multiple of its regulated utility peers.

For the quarter, revenue rose 1% to \$627.9 million, adjusted net earnings declined 49% to \$56.2 million, and adjusted earnings-per-share (“EPS”) fell 50% to \$0.08. And its adjusted EBITDA, a cash flow proxy, fell 4% to \$277.7 million, against Q2 2022. Its regulated utilities segment did well with operating profit climbing 10% to \$255.3 million year over year.

The year-to-date revenue growth was 4% to \$1,406.5 million year over year. The adjusted EPS declined by 31% to \$0.25, while the adjusted EBITDA was essentially flat at \$618.7 million. To be more cautious, we reduced our 2023 EPS estimate to \$0.56.

## Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
<b>EPS</b>	\$0.26	\$0.37	\$0.46	\$0.42	\$0.57	\$0.66	\$0.63	\$0.64	\$0.71	\$0.69	<b>\$0.56</b>	<b>\$0.68</b>
<b>DPS</b>	\$0.33	\$0.37	\$0.49	\$0.55	\$0.60	\$0.51	\$0.55	\$0.61	\$0.67	\$0.71	<b>\$0.43</b>	<b>\$0.53</b>
<b>Shares<sup>1</sup></b>	207	238	256	274	432	489	526	599	654	683	<b>689</b>	<b>761</b>

Investors should note that Algonquin previously paid Canadian dollar-denominated dividends and only started paying a U.S. dollar-denominated dividend in 2014. It also began reporting in US\$ in 2018. So, in the table above, the EPS from 2013 to 2017 are in CAD\$. To match the dividends with the earnings, the dividend-per-share is also displayed in CAD\$ from 2013 to 2017. From 2018 and onwards, the data is in US\$. Historically, Algonquin’s EPS has been volatile. They appeared to stable from 2019 to 2022, as the company increased its scale with a more diversified asset base that was largely regulated utilities with predictable returns or renewable facilities that generate stable cash flow long-term.

Unfortunately, the company was hit by highest interest rates, leading to a higher cost of capital. The successful sale of the renewable portfolio would be a good opportunity to reduce its debt levels. A focused regulated utilities might be able to drive higher growth than what we anticipate (potentially 5-6%). Until the sale actually occurs and Algonquin provides a clear growth outlook, we are maintaining our forecast of an EPS and DPS growth rate of 4.0% through 2028.

<sup>1</sup>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	27.3	22.9	22.4	27.5	22.3	15.7	19.0	22.5	22.6	17.9	12.7	14.0
Avg. Yld.	4.6%	4.4%	4.8%	4.8%	4.7%	4.9%	4.6%	4.2%	4.4%	5.8%	6.1%	5.5%

From 2013-2022, the average price-to-earnings ratio was 22 and the average yield was 4.7%. However, Algonquin's growth is expected to be lower in an environment of higher cost of capital. We also don't expect to trade at a premium valuation like some of its peers. We estimate Algonquin's EPS growth rate to be 4.0% and also have a target price-to-earnings ratio of 14. The stock appears to be about fairly valued. We believe Algonquin would not stray far away from a yield of about 5% in this higher interest rate environment.

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

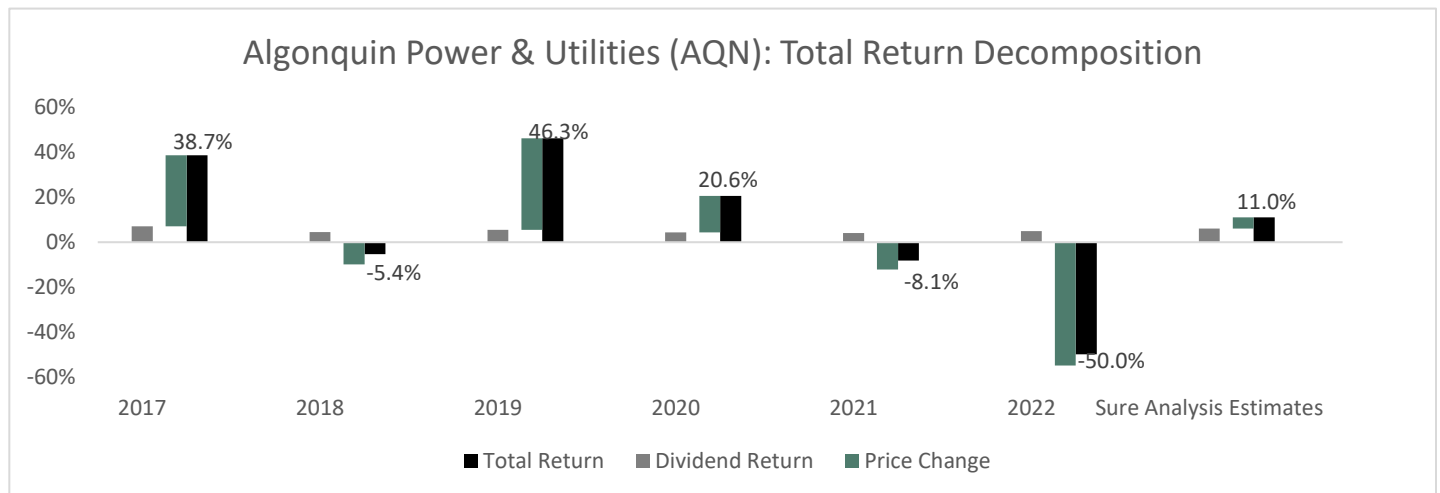
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	127%	100%	107%	131%	105%	77%	87%	95%	94%	103%	78%	78%

Given that Algonquin cut its dividend in 2011 and again in 2023, it's safe to say that it does not have competitive advantages. It cut its dividend in 2011 around the previous recession as earnings fell drastically. Most of the decade displayed payout ratios that were extended. Higher interest rates as well as being a utility that doesn't have the best of balance sheets, it cut its dividend again in 2023. It's not the best time to sell renewable assets, as valuations have gone down from higher interest rates and capital tightening. However, a successful sale can help the company reduce its debt levels and improve its balance sheet. After the 2023 dividend cut, its payout ratio is more sustainable. And we think a 4.0% dividend growth rate is achievable. Algonquin has an investment-grade S&P credit rating of BBB.

## Final Thoughts & Recommendation

Algonquin is a higher-risk utility due to its higher debt levels and higher near-term uncertainties regarding the renewable portfolio and management change. That said, if the company executes well, it could still be a decent investment. Over the next five years, we estimate total returns of 11.0%, coming from a yield of 6.1%, P/E expansion of 2.0%, and earnings growth of 4.0% per year. We rate the stock as a "hold" given the higher risk and that there are better dividend stocks with higher returns potential to consider within the Sure Dividend coverage universe.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Revenue</b>	634	811	741	815	1,522	1,648	1,626	1,677	2,285	2765
<b>Gross Profit</b>	379	449	469	596	1,129	1,164	1,183	1,276	1,566	1899
<b>Gross Margin</b>	59.7%	55.3%	63.3%	73.1%	74.2%	70.6%	72.7%	76.1%	68.5%	68.7%
<b>SG&amp;A Exp.</b>	22	30	29	34	59	53	74	90	83	91
<b>D&amp;A Exp.</b>	93	99	109	146	257	261	284	314	403	456
<b>Operating Profit</b>	97	119	131	174	368	378	353	343	378	500
<b>Operating Margin</b>	15.3%	14.7%	17.7%	21.4%	24.2%	23.0%	21.7%	20.5%	16.6%	18.1%
<b>Net Profit</b>	19	65	85	97	149	185	531	782	265	-212
<b>Net Margin</b>	3.0%	8.0%	11.4%	11.9%	9.8%	11.2%	32.6%	46.7%	11.6%	-7.7%
<b>Free Cash Flow</b>	-56	-206	42	-88	-239	64	30	-281	-1,188	-470
<b>Income Tax</b>	9	14	32	28	73	53	70	65	-43	-62

## Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Total Assets</b>	3,265	3,534	3,597	6,138	8,396	9,399	10,921	13,224	16,786	17628
<b>Cash &amp; Equivalents</b>	13	8	90	82	43	47	62	102	125	58
<b>Accounts Receivable</b>	151	162	135	141	245	246	259	233	301	404
<b>Inventories</b>	31	27	21	28	89	96	91	135	178	225
<b>Goodwill &amp; Int. Ass.</b>	131	126	133	276	1,005	1,009	1,079	1,323	1,306	1417
<b>Total Liabilities</b>	1,888	1,952	1,946	4,288	5,075	5,701	6,514	7,235	9,084	10472
<b>Accounts Payable</b>	14	59	36	67	120	90	150	192	185	186
<b>Long-Term Debt</b>	1,179	1,095	1,071	3,178	3,080	3,337	3,932	4,538	6,211	7512
<b>Shareholder's Equity</b>	788	1,125	1,240	1,272	2,533	2,993	3,691	5,019	5,675	5035
<b>D/E Ratio</b>	1.31	0.84	0.77	2.22	1.13	1.05	1.01	0.87	1.06	1.44

## Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Return on Assets</b>	0.6%	1.9%	2.4%	2.0%	2.1%	2.1%	5.2%	6.5%	1.8%	-1.2%
<b>Return on Equity</b>	2.4%	6.8%	7.2%	7.8%	7.9%	6.7%	15.9%	18.0%	5.0%	-4.0%
<b>ROIC</b>	0.8%	2.5%	3.1%	2.5%	2.6%	2.8%	6.9%	8.3%	2.2%	-1.5%
<b>Shares Out.</b>	207	238	256	274	432	489	526	599	654	677.9
<b>Revenue/Share</b>	3.08	3.75	2.89	2.98	3.94	3.54	3.22	2.97	3.63	4.1
<b>FCF/Share</b>	-0.27	-0.95	0.16	-0.32	-0.62	0.14	0.06	-0.50	-1.89	-0.7

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

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