



Global Water Resources (GWRS)

Updated November 9th, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	\$10.48	5 Year CAGR Estimate:	1.3%	Market Cap:	\$253.3 M
Fair Value Price:	\$7.20	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	11/15/23
% Fair Value:	146%	5 Year Valuation Multiple Estimate:	-7.2%	Payment Date:	11/30/23
Dividend Yield:	2.8%	5 Year Price Target	\$9.64	Years Of Dividend Growth:	8
Dividend Risk Score:	F	Retirement Suitability Score:	F	Rating	Sell

Overview & Current Events

Global Water Resources is a water resource management company that owns, operates, and manages regulated water, wastewater, and recycled water utilities primarily in metropolitan Phoenix, Arizona. The \$253.3 million market-cap company serves more than 74,000 people in 29,000 homes. Global Water generates around \$45 million in annual revenues and pays its dividends on a monthly basis.

On November 8th, 2023, Global Water reported its Q3 results for the period ending September 30th, 2023. For the quarter, revenues increased by 22.2% year-over-year to \$14.5 million. Specifically, growth was driven by an 8.7% increase in active service connections to 61,036, higher rates, and higher consumption. The increase in active service connections was primarily due to new connections associated with the acquisition of Farmers Water in February and a 2.6% organic growth in connections.

EPS came in at \$0.11, up from \$0.07 last year. This increase was due to net income growth of 57.4%. In turn, this was due to revenue growth exceeding the 17.6% increase in operating expenses and the 15.3% increase in interest expenses.

Global Water continues to tap into the fragmented State of Arizona, which is currently amongst the U.S.'s fastest homeownership growth states – hence the consistent organic growth. The company also continues to pursue accretive acquisitions with consolidation benefits and expects continuous growth in connections and rates.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	---	---	---	(\$0.13)	\$0.23	\$0.15	\$0.10	\$0.05	\$0.16	\$0.24	\$0.40	\$0.54
DPS	---	---	---	\$0.260	\$0.27	\$0.277	\$0.288	\$0.288	\$0.292	\$0.295	\$0.30	\$0.33
Shares¹	---	---	---	19.1	19.6	20.5	21.5	22.5	22.6	23.2	24.2	27.0

Global Water has many tailwinds including considerable growth in its recycled water deliveries (7% growth YoY in Q3), notable rate increases, and strong population growth in Phoenix (10.4% over the past decade). As such, we expect EPS to expand massively when expansionary investments slow down. To reflect the stock's actual EPS potential, effectively excluding its current capital-intensive investments, we have used underlying earnings power of \$0.40, growing by a rate of 6% annually through 2028. Note that this is a 'potential' figure, rather than something that's likely to materialize this year. Wall Street consensus EPS estimate for the year is \$0.31.

In terms of its dividend, the company uses a complex financing strategy. Since the underlying net income does not cover dividends, management had been consistently issuing shares and using the proceeds to pay the monthly dividend. In a sense, the monthly dividend plays the role of interest paid to shareholders for “lending” their funds to the company. While this strategy would not be sustainable in the long-term, the company expects to see significant EPS growth over the next few years, as its growth eventually matures and net income catches up to the dividends paid. Management has been growing the dividend annually by fractions (0.8% most recently) as a token to shareholders for their patience as the company drains its margins in order to grow. Consequently, we expect DPS to continue growing by no more than 2%

¹ Share count is in millions.

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annually in the medium-term. Not only can Global Water not afford it, but to issue additional shares at a faster rate would be arguably too dangerous to pull-off under its already quite complex financing strategy.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	---	---	---	---	---	---	---	---	---	---	26.2	18.0
Avg. Yld.	---	---	---	1.3%	2.8%	2.8%	2.7%	1.9%	1.6%	1.9%	2.8%	3.4%

The company's past P/E ratios are not meaningful due to management's strategy mentioned above. The stock is currently trading at a P/E of 26.2 based on our speculative earnings power. Shares appear much more expensive based on reported earnings. We lower our fair P/E to 18, from 20 previously. The drop is to reflect mid-single-digit EPS growth prospects, as well as the rise in interest rates. Investors appear to appreciate the secured cash flows that come from water being an essential utility and the regulatory rate increases, but we still find the stock very expensive. Shares offer a dividend yield of 2.8%, which remains rather underwhelming despite the recent correction in the stock price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

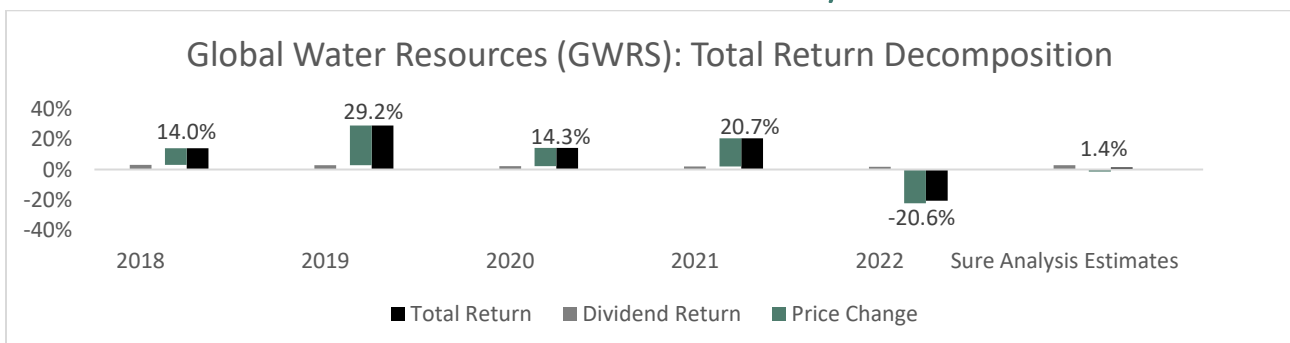
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	---	---	---	---	117%	185%	288%	576%	182%	123%	74%	61%

To claim that Global Water's dividends are safe would be reckless. Management is leveraging its business's highly-secure cash flows to make this work, and while it is currently working, payout safety is largely speculative. The company's strategy of issuing shares in order to pay dividends is not exactly a textbook financing case. Still, the company is growing in one of the most attractive cities, benefiting from robust organic growth and the industry's stability. We believe that the company is subject to minor operational risks and should continue expanding. Its history as a trading company is not that long, however cash flows should remain robust even under a heavy recession. Further, the company should not face significant competition going forward, as water provision is a regulated capital-intensive business.

Final Thoughts & Recommendation

Global Water is a truly unique case. The company is benefiting from several catalysts, including organic growth, amid operating in one of the U.S.'s fastest-growing areas. Consequently, the company is able to request above-average rate increases while enjoying robust cash flows due to its business model. However, management's capital allocation strategy may be too exotic for some investors. Since our expected EPS forecast is quite speculative, our expected returns remain quite speculative as well. As more quarters pass by, our estimates should grow more accurate. In any case, we are currently estimating there are no gains to be made over the next few years as investors likely continue to overvalue the company. Our case has held true since initiating coverage of the stock, which we continue to rate as a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	---	33	32	30	31	36	35	38.6	41.9	45
Gross Profit	---	22	23	22	24	27	27	29.1	31.6	34
Gross Margin	---	68.0%	71.0%	73.0%	75.8%	76.8%	74.9%	75.4%	75.4%	75.6%
SG&A Exp.	---	9	8	10	9	11	11	12.7	15.2	16
D&A Exp.	---	9	8	6	7	7	8	9	9.5	10
Operating Profit	---	55	7	6	7	9	7	7.3	7	8
Operating Margin	---	168.3%	20.4%	19.5%	23.5%	26.1%	19.6%	18.9%	16.7%	17.8%
Net Profit	---	65	21	(3)	5	3	2	1.1	3.6	5.5
Net Margin	---	199.4%	66.9%	-8.4%	14.6%	8.7%	6.3%	2.8%	8.6%	12.2%
Free Cash Flow	---	10	1	(7)	(10)	7	0	5.4	2.1	(11)
Income Tax	---	(17)	21	(1)	(1)	2	1	0.8	1.2	1

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	---	308	236	239	239	262	266	283	294	323
Cash & Equivalents	---	7	12	20	5	13	8	18	12.6	7
Accounts Receivable	---	1	1	1	2	1	2	2.5	2.2	2.6
Inventories	---	---	---	---	---	---	---	---	---	---
Goodwill & Int. Ass.	---	26	13	13	13	16	17	16	16.1	15
Total Liabilities	---	280	216	224	224	235	241	251	264	279
Accounts Payable	---	2	1	2	0	1	1	0.5	2.1	2.2
Long-Term Debt	---	130	104	114	114	114	114	114	113	109
Shareholder's Equity	---	28	20	15	15	28	25	32	30	44
LTD/E Ratio	---	4.69	5.19	7.62	7.70	4.11	4.64	3.56	3.75	2.45

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	---	---	7.9%	-1.1%	1.9%	1.2%	0.8%	---	1.3%	1.8%
Return on Equity	---	---	89.5%	-14.3%	30.5%	14.5%	8.5%	---	11.6%	14.8%
ROIC	---	---	15.2%	-2.0%	3.5%	2.3%	1.6%	---	2.5%	3.7%
Shares Out.	---	---	---	19.1	19.6	20.5	21.5	---	22.9	23.3
Revenue/Share	---	1.68	1.65	1.56	1.59	1.73	1.65	---	1.83	1.92
FCF/Share	---	0.51	0.05	(0.35)	(0.50)	0.32	0.02	---	0.09	(0.5)

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

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