American Water Works Company, Inc. (AWK)

Updated February 15th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	$122	**5 Year CAGR Estimate:**	8.9%	**Market Cap:**	$23.8 B
Fair Value Price:	$116	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	02/07/2024
% Fair Value:	106%	**5 Year Valuation Multiple Estimate:**	-1.2%	**Dividend Payment Date:**	03/01/2024
Dividend Yield:	2.3%	**5 Year Price Target**	$170	**Years Of Dividend Growth:**	15
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Rating:**	Hold

Overview & Current Events

American Water Works is the largest and most geographically diverse, publicly traded water and wastewater utility company in the United States, as measured by both operating revenues and population served. The company provides drinking water, wastewater, and other related services to over 15 million people in 46 states. Its regulated business includes 53,700 miles of pipe, 490 water treatment plants, 175 wastewater facilities, 1200 wells, and 74 dams. The company also provides water and related services to the U.S. government and U.S. military through 17 installations. American Water Works generates around $4.23 billion in annual revenues and based in Camden, New Jersey.

On February 14th, 2024, American Water Works reported its Q4 and full-year results for the period ending December 31st, 2023. For the quarter, revenues rose by 10.9% year-over-year to $1.03 billion. The increase in revenues was primarily a result of i) authorized revenue increases from completed general rate cases and ii) infrastructure proceedings for the recovery of incremental capital and acquisition investments.

EPS came in at $0.88 compared to $0.81 last year, driven by a 16.3% increase in net income due to higher revenues, partially offset by a higher share count. The company now has general rate cases in progress in eight jurisdictions and has filed for infrastructure surcharges in one jurisdiction, reflecting a total annualized revenue request of approximately $670 million. For FY2024, management raised their forecast, expecting EPS to land between $5.20 and $5.30, up from $5.10 to $5.20. They also affirmed their long-term EPS growth outlook of between 7% and 9%.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$2.36	$2.66	$2.63	$2.39	$3.15	$3.43	$3.91	$6.96	$4.51	$4.90	***$5.25***	***$7.71***
DPS	$1.21	$1.33	$1.47	$1.62	$1.78	$1.96	$2.15	$2.36	$2.57	$2.78	***$2.83***	***$4.16***
Shares[1]	180	180	179	179	180	181	181	182	182	195	***195***	***200***

American Water Works has a highly stable and robust track record both in terms of its profitability and its dividend payments. The company enjoys an extremely resilient business model due to water being a necessity both for residential and industrial usage, as well as a mission-critical asset for the military. As a result, American Water has been able to grow its network and operations with limited risks. Over the next nine years, the company expects to invest approximately $30 billion in renewing its infrastructure, achieving operational efficiencies through new technologies, ensuring water quality, and expanding its overall operations. Management continues to expect EPS to grow by approximately 7%-9% annually through 2029, powered by 5%-7% from regulated investment CAPEX, 1.5%-2.5% from regulated acquisitions, and <1% from military services. EPS growth includes rate base increases which the company estimates to grow by a CAGR of 8%-9% through 2031.

We have utilized an EPS CAGR of 8.0% in our calculations, which is the mid-point of management's guidance. The dividend has grown annually over the past 15 years, displaying at 5 and 10-year CAGR of 7.6% and 9.7%, respectively. Management intends to grow the dividend between a rate of 7% and 10% through 2029. Thus, we have set our expected growth rate at 8% through 2029.

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[1] Share count is in millions.

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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	20.3	19.2	28.5	32.2	27.3	33.8	32.7	24.4	34.4	28.5	***23.3***	***22.0***
Avg. Yld.	2.5%	2.6%	2.0%	2.1%	2.1%	1.7%	1.7%	1.4%	1.7%	2.0%	***2.3%***	***2.5%***

American Water Works' valuation has hovered at rather inflated levels over the past decade. This has also been the case with all of the company's industry peers, which have also traded at quite rich multiples. We believe this is due to Wall St. treating water stocks (along with their dividends) as ultra-safe investments due to their high operational predictability. Due to higher interest rates, most water stocks, along with AWK, have experienced a correction in their valuation multiples lately. Despite the company's fantastic qualities and predictable growth prospects, we believe that a further compression is possible given the stock's modest yield.

Safety, Quality, Competitive Advantage, & Recession Resiliency

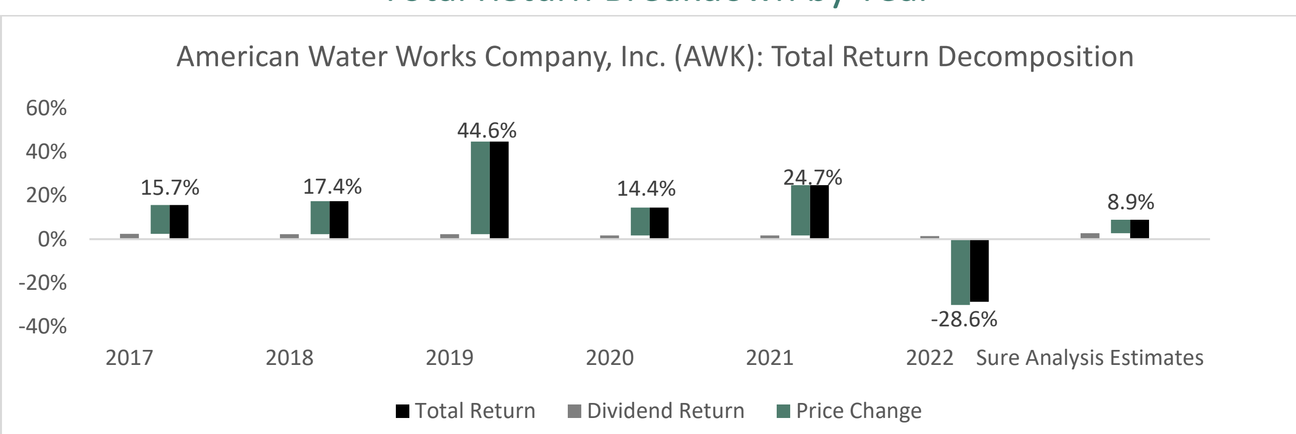
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	51%	50%	56%	68%	57%	57%	55%	34%	57%	57%	***54%***	***54%***

American Water's dividend can be viewed as extremely safe. The payout ratio stands at 54%, and the company has a very clear and predictable path towards growing its EPS. Its cash flows are of high quality due to water being an essential commodity, with much-anticipated consumption rates and robust pricing power. Additionally, the company enjoys a rock-solid competitive advantage, operating in an oligopolistic industry, which is also very capital intensive and hence almost forbids new market participants. The company is the biggest amongst its peers, while its relationship with the government also adds to its already great moat. We expect American Water to deliver resilient results even through a prolonged recession. The company is not meaningfully correlated to the underlying economy. Hence, the excellent results during 2020 and 2021 despite COVID-19.

Final Thoughts & Recommendation

American Water Works comes with several attractive characteristics. That being said, the company's secure business model and incredibly predictable cash flows and growth trajectory have caused the stock's valuation to remain modestly elevated. Based on management's reaffirmed medium-term guidance and our valuation compression forecast, we estimate annualized returns of around 8.9% through 2029. Thus, we have assigned a hold rating to the stock. We highlight that AWK offers one of the most predictable future total return-return profiles amongst dividend-paying stocks.

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	2,879	3,011	3,159	3,302	3,357	3,440	3,610	3,777	3,930	3,792
Gross Profit	1,590	1,661	1,755	1,803	1,988	1,961	2,066	2,155	2,153	2,203
Gross Margin	55.2%	55.2%	55.6%	54.6%	59.2%	57.0%	57.2%	57.1%	54.8%	58.1%
D&A Exp.	407	424	440	470	492	545	582	604	636	649
Operating Profit	949	1,001	1,072	1,075	1,237	1,139	1,204	1,248	1,196	1,273
Operating Margin	33.0%	33.2%	33.9%	32.6%	36.8%	33.1%	33.4%	33.0%	30.4%	33.6%
Net Profit	369	423	476	468	426	567	621	709	1,263	820
Net Margin	12.8%	14.0%	15.1%	14.2%	12.7%	16.5%	17.2%	18.8%	32.1%	21.6
Free Cash Flow	(149)	63	(72)	(106)	(61)	(287)	(375)	(502)	(432)	(1312)
Income Tax	237	280	306	302	486	222	212	215	377	188

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	15,088	16,038	17,241	18,482	19,482	21,223	22,682	24,766	26,080	28
Cash & Equivalents	27	23	45	75	55	130	60	547	116	85
Accounts Receivable	208	232	255	269	272	301	294	321	271	334
Inventories	33	37	38	39	41	41	44	47	57	98
Goodwill & Int. Ass.	1,208	1,208	1,302	1,345	1,388	1,659	1,568	1,559	1,139	1,143
Total Liabilities	10,360	11,123	12,192	13,264	14,097	15,359	16,561	18,312	18,780	20,090
Accounts Payable	264	100	126	154	195	175	203	189	235	254
Long-Term Debt	5,857	5,938	6,544	7,172	7,717	8,604	9,453	10,940	10,980	12,380
Shareholder's Equity	4,728	4,915	5,049	5,218	5,385	5,864	6,121	6,454	7,298	7,693
LTD/E Ratio	1.24	1.21	1.30	1.37	1.43	1.47	1.54	1.70	1.51	1.61

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	2.5%	2.7%	2.9%	2.6%	2.2%	2.8%	2.8%	3.0%	5.0%	3.0%
Return on Equity	8.0%	8.8%	9.6%	9.1%	8.0%	10.1%	10.4%	11.3%	18.4%	10.9%
ROIC	3.6%	3.9%	4.2%	3.9%	3.3%	4.1%	4.1%	4.3%	7.1%	4.3%
Shares Out.	179	180	180	179	179	180	181	182	182	182
Revenue/Share	16.08	16.73	17.55	18.45	18.75	19.11	19.94	20.75	21.59	20.84
FCF/Share	(0.83)	0.35	(0.40)	(0.59)	(0.34)	(1.59)	(2.07)	(2.76)	(2.37)	(7.21)

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