



Canadian Utilities (CDUAF)

Updated March 10th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	\$22.97	5 Year CAGR Estimate:	9.1%	Market Cap:	\$6.24B
Fair Value Price:	\$23.22	5 Year Growth Estimate:	4.0%	Ex-Dividend Date:	05/03/2024 ¹
% Fair Value:	99%	5 Year Valuation Multiple Estimate:	0.2%	Dividend Payment Date:	06/03/2024
Dividend Yield:	5.8%	5 Year Price Target	\$28	Years Of Dividend Growth²:	52
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating	Hold

Overview & Current Events

Canadian Utilities is a \$6.24 billion company with approximately 5,000 employees. ATCO owns 53% of Canadian Utilities. Based in Alberta, Canadian Utilities is a diversified global energy infrastructure corporation delivering solutions in Electricity, Pipelines & Liquid, and Retail Energy. The company prides itself on having Canada's longest consecutive years of dividend increases, with a 52-year streak. Unless otherwise noted, US dollars are used in this research report.

On January 12th, 2024, Canadian Utilities increased its dividend by 1% to a quarterly rate of C\$45.3. The annualized rate of C\$1.812 equals close to US\$ of \$1.34 at the current FX rates.

On February 29th, 2024, Canadian Utilities posted its Q4 and full-year results for the period ending December 31st, 2023. Revenues for the year amounted to \$2.87 billion, 6.2% lower year-over-year (in constant currency), while adjusted EPS came in at \$1.64, about 9% lower year-over-year. GAAP EPS came in at \$1.76, up from \$1.53 in FY2022.

Lower revenues stemmed from cost efficiencies in Electricity and Natural Gas Distribution under the second-generation Performance Base Regulation (PBR), which were passed on to customers in the 2023 Cost of Service (COS) rebasing. The decision by the Alberta Utilities Commission (AUC) to collect 2021 deferred revenues in 2022, coupled with lower retail prices in ATCO Energy, also contributed. Partially offsetting these factors were increased revenues from ATCO EnPower's acquired wind assets, higher flow-through revenues in Electricity Distribution, and elevated rates and system volumes in International Natural Gas Distribution.

The reason adjusted EPS declined while GAAP EPS rose was due to GAAP EPS benefiting from \$139 million in unrealized gains on mark-to-market forward and swap commodity contracts. Our initial estimates point to EPS of \$1.72 for FY2024.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	\$2.18	\$0.81	\$1.54	\$1.32	\$1.53	\$2.50	\$1.04	\$0.96	\$1.53	\$1.76	\$1.72	\$2.09
DPS	\$0.92	\$0.85	\$0.97	\$1.14	\$1.15	\$1.30	\$1.37	\$1.39	\$1.31	\$1.35	\$1.34	\$1.52
Shares³	262	265	267	269	272	273	273	270	269	270	270	270

By benefiting from a stable business model, Canadian Utilities can slowly, but progressively, grow its earnings. The company consistently invests in new projects and benefits from the base rate increases, which grow at around 3% to 4% annually. In 2021, management had filed an application with the Alberta Utilities Commission to postpone Canadian Utilities' electricity and natural gas distribution rate increases.

The company received almost all deferred revenues by the end of 2022. Combining the company's growth projects and the possibility of modest margin improvements, we retain our projected growth rate at 4%. Our DPS CAGR estimate remains at 2.5%. The company will likely improve its payout ratio before its new projects start producing enough cash flows to re-accelerate dividend growth. U.S. investors have enjoyed a lesser growth in their dividends than the Canadian

¹ Estimated dates based on past dividend dates

² Years of Dividend Growth and Last Dividend Increase based in C\$.

³ Share count in millions

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ones over the past decade due to the depreciation of \$CAD to \$USD. Regardless, the stock's impressive 10-year dividend CAGR of 9.6% is more than enough to compensate for the FX fluctuations, progressively growing investors' income.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	18.1	19.3	20.9	18.3	18.2	15.0	22.9	16.5	17.9	14.3	13.4	13.5
Avg. Yld.	2.7%	3.4%	3.6%	3.5%	4.6%	4.8%	4.8%	4.8%	4.8%	5.4%	5.8%	5.4%

Canadian Utilities' shares currently yield an attractive 5.8%, a notable high for this legendary dividend payer. This above-average yield can be attributed to the current decade-high interest rates, prompting investors to value YieldCos at higher yields.

The stock's current P/E ratio of 13.4 is notably below its historical average of about 18. However, again, we believe that the multiple compression is well-justified given the rapid increases in interest rates. Investors demand higher tangible returns in the face of higher risk-free returns from T-bills. Thus, we believe the current, more humble valuation will last.

Safety, Quality, Competitive Advantage, & Recession Resiliency

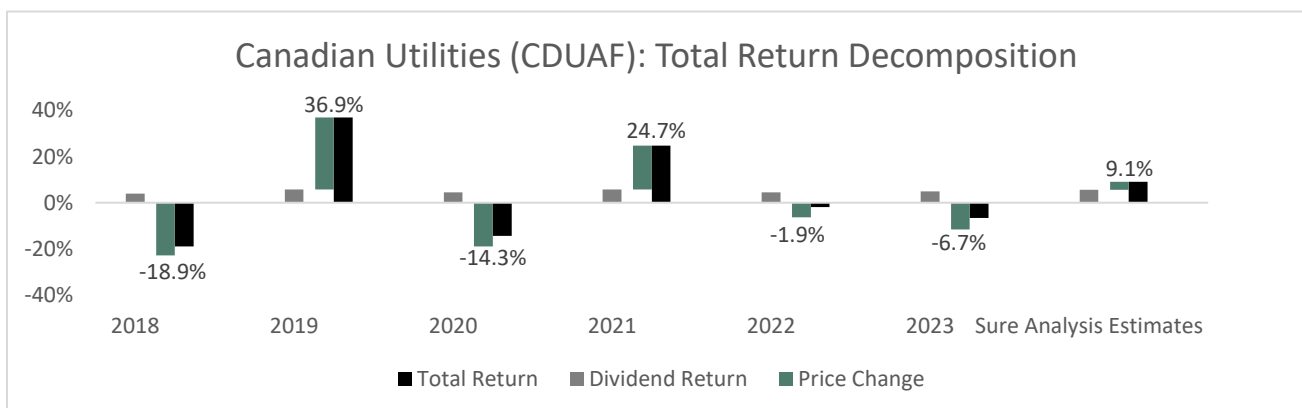
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	42%	105%	63%	86%	75%	52%	132%	145%	86%	77%	78%	72%

The company's competitive advantage lies in the moat regulated utilities are surrounded by. With no easy entry in the sector, regulated utilities enjoy an oligopolistic market with little competition threat. The company's resiliency has been proven for decade after decade. Despite multiple recessions and uncertain environments over the half a century, the company has withstood every one of them while raising its dividend. While Canadian Utilities' payout ratio were under pressure during 2020 (though dividends were in reality covered from its operating cash flows if we are to exclude depreciation and amortization,) by 2029 we expect it to have returned to more comfortable levels, of around 72% of its net income.

Final Thoughts & Recommendation

We believe that Canadian Utilities is an excellent hold for income-oriented investors who seek stable and predictable returns. The above-average dividend yield is quite attractive, and we believe that Canadian Utilities offers low volatility and a stable investment case during a time of high uncertainty. However, share prices are likely to remain muted in the current interest-rates environment. We project annualized returns of 9.1%, driven by the 5.8% dividend yield, modest EPS growth expectations, and relatively stable valuation assumptions. Shares earn a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	\$3,283	\$3,261	\$2,557	\$2,567	\$3,152	\$3,378	\$2,942	\$2,413	2,804	3,111
Gross Profit	\$2,266	\$2,137	\$1,910	\$2,009	\$2,144	\$2,240	\$2,188	\$1,877	1,891	2,101
Gross Margin	69.0%	65.5%	74.7%	78.3%	68.0%	66.3%	74.4%	77.8%	67.4%	67.5%
SG&A Exp.	\$498	\$463	\$363	\$293	\$272	\$330	\$258	\$255	289	287
D&A Exp.	\$464	\$466	\$503	\$433	\$461	\$492	\$439	\$455	519	493
Operating Profit	\$1,033	\$922	\$639	\$898	\$917	\$835	\$963	\$702	696	870
Operating Margin	31.5%	28.3%	25.0%	35.0%	29.1%	24.7%	32.7%	29.1%	24.8%	28.0%
Net Profit	\$570	\$644	\$276	\$468	\$397	\$489	\$717	\$319	313	486
Net Margin	17.4%	19.8%	10.8%	18.2%	12.6%	14.5%	24.4%	13.2%	11.2%	15.6%
Free Cash Flow	-\$517	-\$596	-\$43	\$248	\$73	-\$205	\$185	\$553	396	593
Income Tax	\$182	\$187	\$161	\$178	\$133	\$174	\$40	\$113	110	153

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	14,135	14,388	13,021	13,945	16,572	16,020	15,344	15,920	16,530	16,190
Cash & Equivalents	\$468	\$302	\$350	\$256	\$304	\$400	\$745	\$609	585	514
Accounts Receivable	\$448	\$418	\$312	\$384	\$469	\$496	\$389	\$426	507	620
Inventories	\$85	\$73	\$32	\$28	\$32	\$23	\$23	\$22	16	18
Goodwill & Int. Ass.	\$347	\$341	\$349	\$390	\$448	\$463	\$482	\$514	569	603
Total Liabilities	\$9,070	\$9,558	\$8,558	\$9,294	\$11,530	\$11,202	\$10,046	\$10,580	11,180	10,980
Long-Term Debt	\$5,910	\$6,305	\$5,759	\$6,214	\$7,890	\$7,694	\$6,864	\$7,102	7,464	7,029
Shareholder's Equity	\$4,019	\$3,870	\$3,259	\$3,401	\$3,714	\$3,592	\$4,020	\$4,029	3,972	3,911
LTD/E Ratio	1.17	1.31	1.33	1.38	1.61	1.64	1.33	1.37	1.43	1.39

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	4.2%	4.5%	2.0%	3.5%	2.6%	3.0%	4.6%	2.0%	1.9%	3.0%
Return on Equity	14.8%	16.3%	7.7%	14.1%	11.1%	13.4%	18.8%	7.9%	7.8%	12.3%
ROIC	5.5%	5.8%	2.6%	4.4%	3.3%	3.8%	5.8%	2.6%	2.5%	3.9%
Shares Out.	259.3	262.8	265.3	267.8	270.1	272.1	273.2	273	270	270
Revenue/Share	\$12.66	\$12.41	\$9.64	\$9.59	\$11.67	\$12.41	\$10.77	\$8.83	10.37	11.51
FCF/Share	-\$1.99	-\$2.27	-\$0.16	\$0.93	\$0.27	-\$0.75	\$0.68	\$2.02	1.47	2.19

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

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