



# California Water Services (CWT)

Updated November 4<sup>th</sup>, 2024 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$50	<b>5 Year CAGR Estimate:</b>	12.7%	<b>Market Cap:</b>	\$2.9B
<b>Fair Value Price:</b>	\$66	<b>5 Year Growth Estimate:</b>	5.0%	<b>Ex-Dividend Date:</b>	02/03/25 <sup>1</sup>
<b>% Fair Value:</b>	76%	<b>5 Year Valuation Multiple Estimate:</b>	5.7%	<b>Dividend Payment Date:</b>	02/08/25 <sup>2</sup>
<b>Dividend Yield:</b>	2.2%	<b>5 Year Price Target</b>	\$84	<b>Years Of Dividend Growth:</b>	56
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	B	<b>Rating:</b>	Buy

## Overview & Current Events

California Water Service is the 3<sup>rd</sup> largest publicly-owned water utility in the United States. The company has six subsidiaries that provide water to about two million people, mainly in California, with some additional operations in Washington, New Mexico, and Hawaii. California Water Service was founded in 1926 and has increased its dividend for more than 50 consecutive years, which makes the company a Dividend King.

California Water Service reported its third quarter earnings results on October 31. The company reported that its operating revenues totaled \$300 million during the quarter, which was 18% more than the revenues that California Water Service generated during the previous year's quarter. This represents a stronger performance compared to what the analyst community had forecasted. The operating revenue increase was driven by rate increases over the last year as well as by higher accrued unbilled revenue compared to the previous year's quarter.

California Water Service generated earnings-per-share of \$1.03 during the third quarter, which was slightly worse than what was expected by the analyst community. California Water Services is generally most profitable during the summer quarter, when water demand is way higher than during the winter quarters, thus healthy profits during the period are in line with historic patterns. Profits during 2024 should hit a new record high per current estimates.

## Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
<b>EPS</b>	\$1.19	\$0.94	\$1.01	\$1.52	\$1.36	\$1.31	\$1.97	\$1.96	\$1.77	\$0.89	<b>\$3.30</b>	<b>\$4.21</b>
<b>DPS</b>	\$0.65	\$0.67	\$0.69	\$0.72	\$0.75	\$0.79	\$0.85	\$0.92	\$1.00	\$1.04	<b>\$1.12</b>	<b>\$1.50</b>
<b>Shares<sup>3</sup></b>	48	48	48	48	48	48	50	53	55	57	<b>58</b>	<b>60</b>

Between 2014 and 2022, California Water Service grew its earnings-per-share at an average annual rate of 5%, which is a decent pace of earnings growth for a utility, while earnings-per-share took a hit in 2023 due to some one-time effects. Earnings-per-share are very seasonal for California Water. The second and third quarters are usually significantly more profitable than the rest of the year, as demand for fresh water is significantly higher during the very warm summer months in California when consumers use more water, e.g. for watering their lawns.

During the Great Recession, California Water Service's earnings-per-share did not decline meaningfully, as earnings-per-share dropped by just 4% between 2008 and 2010. This is not surprising, as consumption behavior and demand for fresh water is more reliant upon the weather than on the strength of the overall economy.

We believe that California Water Service's earnings-per-share will continue to grow at a mid-single-digits rate going forward, as it did in the past. Earnings growth in the long run should be achievable thanks to the rate hikes that are regularly approved by regulators. Regulators need to continuously encourage the company to keep investing in the expansion and maintenance of its network, as its customers are dependent on high-quality infrastructure that will remain reliable in the future, which is why future rate increases are more or less a given.

<sup>1</sup> Estimated date

<sup>2</sup> Estimated date

<sup>3</sup> 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	19.7	24.8	29.6	26.9	35.3	39.7	27.4	36.7	34.5	58.4	15.2	20.0
Avg. Yld.	2.8%	2.9%	2.3%	1.9%	1.6%	1.5%	1.6%	1.3%	1.6%	2.0%	2.2%	1.8%

California Water Service has never been a high-growth stock, but the resilience during economic downturns and the relatively predictable earnings and dividend growth have made it appropriate for risk-averse investors. The valuation of the company's shares has expanded significantly through 2023, but due to much higher expected profits in 2024, the earnings multiple for this year is pretty low compared to the historic range. For the first time in many years, California Water Service is not overvalued any more, and trades below fair value right now.

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

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	54.6%	71.3%	68.3%	51.4%	55.1%	60.3%	43.1%	46.9%	56.5%	117%	33.9%	35.6%

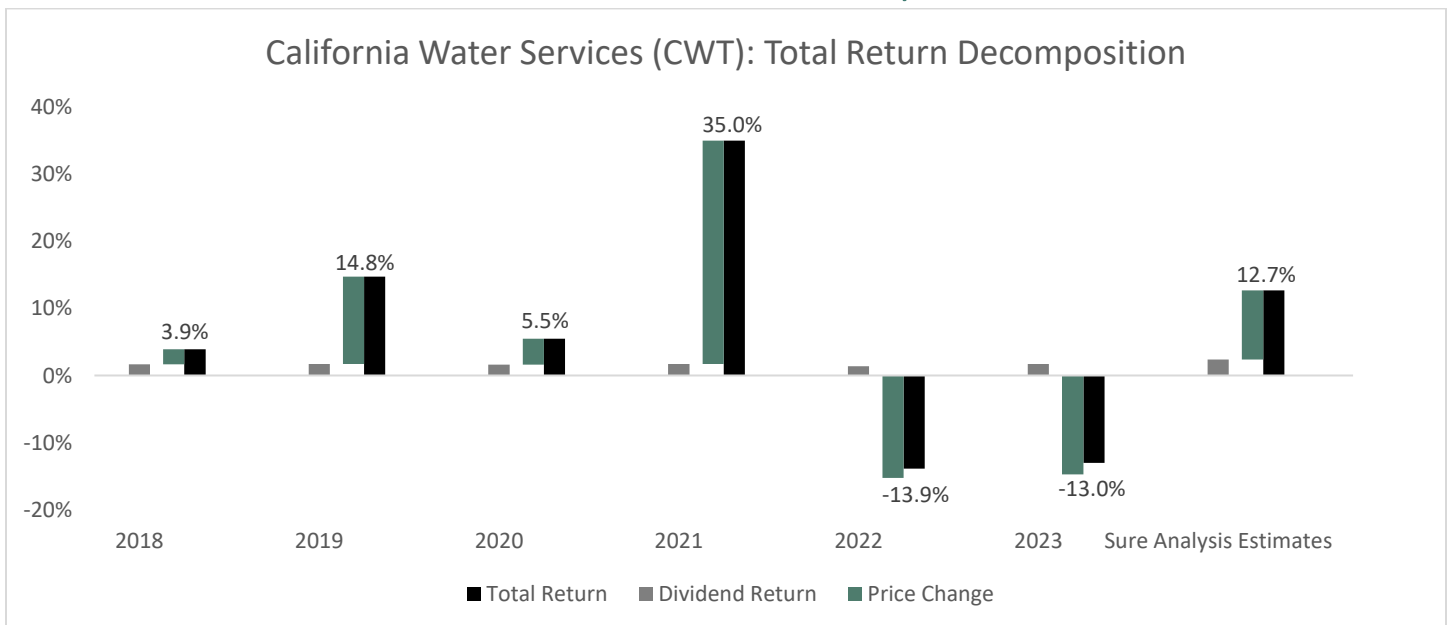
California Water Service has paid out between 40% and 70% of its net profits throughout most of the last decade. The dividend payout ratio has seen some major ups and downs over that time, with 2023 being an outlier with a payout ratio of more than 100%. With earnings-per-share recovering substantially in 2024, the dividend looks very sustainable again, and the fact that the company has increased its dividend for more than five decades is very encouraging.

California Water Service is a regulated utility, and as such, it does not have to worry about competition too much. The company is not vulnerable to recessions or economic downturns, as consumers need fresh water no matter the strength of the economy. Weather conditions/temperature can impact results, though, and are unpredictable.

## Final Thoughts & Recommendation

As a regulated water utility, California Water Service operates in a relatively unspectacular industry. This is not necessarily a negative for investors, as businesses like these can still be strong and reliable investments when bought at the right price. California Water Service looks like a compelling investment today, trading below fair value and offering double-digit total returns per year from the current level. We thus rate California Water Service a buy right now.

## 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>	597	588	609	676	698	715	794	791	846	795
<b>Gross Profit</b>	288	292	286	337	341	341	392	271	281	221
<b>Gross Margin</b>	48.2%	49.6%	47.0%	49.9%	48.8%	47.7%	49.3%	34.2%	33.3%	27.8%
<b>SG&amp;A Exp.</b>	97	113	88	93	101	109	117	0	0	0
<b>D&amp;A Exp.</b>	63	63	65	79	86	91	101	112	117	123
<b>Operating Profit</b>	109	96	112	146	133	121	151	132	136	69
<b>Operating Margin</b>	18.2%	16.3%	18.4%	21.6%	19.1%	17.0%	19.0%	16.7%	16.1%	8.7%
<b>Net Profit</b>	57	45	49	73	66	63	97	101	96	52
<b>Net Margin</b>	9.5%	7.7%	8.0%	10.8%	9.4%	8.8%	12.2%	12.8%	11.3%	6.5%
<b>Free Cash Flow</b>	(4)	(32)	(68)	(111)	(93)	(105)	(181)	(61)	(84)	(166)
<b>Income Tax</b>	28	25	27	37	16	18	12	4	6	(7)

## Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Total Assets</b>	2,187	2,241	2,412	2,745	2,838	3,111	3,394	3,623	4,265	4,596
<b>Cash &amp; Equivalents</b>	20	9	25	95	47	43	45	78	62	40
<b>Accounts Receivable</b>	26	32	30	32	30	32	53	68	62	66
<b>Inventories</b>	6	6	6	6	7	8	9	10	13	16
<b>Goodwill &amp; Int. Ass.</b>	14	15	14	25	27	27	59	67	54	58
<b>Total Liabilities</b>	1,561	1,599	1,752	2,045	2,108	2,331	2,473	2,451	2,942	3,165
<b>Accounts Payable</b>	59	66	78	94	96	108	132	144	141	157
<b>Long-Term Debt</b>	505	548	655	807	880	984	1,156	1,096	1,126	1,233
<b>Shareholder's Equity</b>	627	642	659	699	730	780	921	1,167	1,318	1,427
<b>LTD/E Ratio</b>	0.81	0.85	0.99	1.15	1.21	1.26	1.25	0.94	0.85	0.86

## Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Return on Assets</b>	2.7%	2.0%	2.1%	2.8%	2.3%	2.1%	3.0%	2.9%	2.4%	1.2%
<b>Return on Equity</b>	9.3%	7.1%	7.5%	10.7%	9.2%	8.4%	11.4%	9.7%	7.7%	3.8%
<b>ROIC</b>	5.1%	3.9%	3.9%	5.2%	4.2%	3.7%	5.0%	4.7%	4.1%	2.0%
<b>Shares Out.</b>	48	48	48	48	48	48	50	53	55	57
<b>Revenue/Share</b>	12.49	12.29	12.71	14.08	14.53	14.83	16.12	15.32	15.57	13.95
<b>FCF/Share</b>	(0.08)	(0.67)	(1.43)	(2.32)	(1.93)	(2.18)	(3.67)	(1.19)	(1.54)	(2.91)

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

### Disclaimer

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