



Global Water Resources (GWR)

Updated November 12th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	\$12.92	5 Year CAGR Estimate:	-2.8%	Market Cap:	\$312.9 M
Fair Value Price:	\$7.20	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	11/13/24
% Fair Value:	179%	5 Year Valuation Multiple Estimate:	-11.0%	Payment Date:	11/27/24
Dividend Yield:	2.3%	5 Year Price Target	\$9.64	Years Of Dividend Growth:	9
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. As of the end of last year, Global Water Resources served more than 82,000 people in 32,000 homes. Global Water generates around \$53 million in annual revenues and pays its dividends on a monthly basis.

On November 6th, 2024, Global Water reported its Q3 results for the period ending September 30th, 2024. Quarterly revenues fell by 1.5% year-over-year to \$14.3 million. The drop in revenue was mainly attributable to the recognition of \$0.5 million in unregulated revenue related to infrastructure coordination and financing agreements (ICFAs) in the third quarter of 2023 that did not recur this time around. Still, regulated revenue increased 2.2% to \$14.3 million, primarily due to total active service connections rising 4.7% to 63,889.

EPS came in at \$0.12, up one cent year-over-year despite the decline in total revenues, due to operating expenses falling by 3.3% to \$10.3 million. This was, in turn, due to lower depreciation and amortization expense, personnel related costs, information technology expense and professional fees.

Global Water continues to tap into the fragmented state of Arizona, which is currently amongst the U.S.'s fastest homeownership growth rates – 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	---	---	(\$0.13)	\$0.23	\$0.15	\$0.10	\$0.05	\$0.16	\$0.24	\$0.33	\$0.30	\$0.54
DPS	---	---	\$0.26	\$0.27	\$0.28	\$0.29	\$0.29	\$0.29	\$0.30	\$0.30	\$0.30	\$0.33
Shares¹	---	---	19.1	19.6	20.5	21.5	22.5	22.6	23.2	24.0	24.3	27.0

Global Water has many tailwinds including considerable growth in its recycled water deliveries (6% growth YoY in Q1), notable rate increases, and strong population growth in Phoenix. 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 2029. 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 \$0.30.

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

¹ Share count is in millions.

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been growing the dividend annually by fractions (1.2% 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 keep growing by no more than 2%.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	---	---	---	---	---	---	---	---	---	---	32.3	18.0
Avg. Yld.	---	---	1.3%	2.8%	2.8%	2.7%	1.9%	1.6%	1.9%	2.8%	2.3%	3.5%

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 32.3 based on our speculative earnings power. Shares appear much more expensive based on reported earnings. We maintain our fair P/E to 18. Our discount is to reflect the soft, 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 2.3%, which remains rather underwhelming.

Safety, Quality, Competitive Advantage, & Recession Resiliency

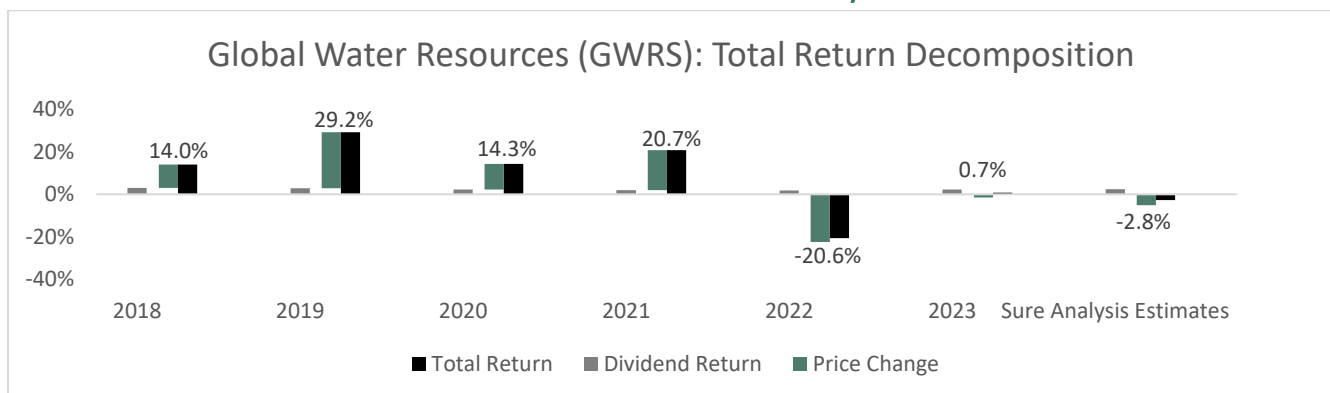
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	---	---	---	117%	185%	288%	576%	182%	123%	90%	75%	62%

To claim that Global Water's dividends are safe would be reckless. Management is leveraging its business's highly-secure cash flows to make it work and, while it is currently working, payout safety is largely speculative. Their 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 solid organic growth and the industry's stability. We believe that Global Water is subject to minor operational risks and should continue expanding. Its history as a public company is not that long. Still, 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. Still, 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. In any case, we are currently estimating that shareholders will see a loss of 2.8% per year over the next five years as the market is likely to continue to overvalue the company. Our expectation 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	33	32	30	31	36	35	38.6	41.9	45	53
Gross Profit	22	23	22	24	27	27	29.1	31.6	34	40
Gross Margin	68.0%	71.0%	73.0%	75.8%	76.8%	74.9%	75.4%	75.4%	75.6%	75.5%
SG&A Exp.	9	8	10	9	11	11	12.7	15.2	16	17
D&A Exp.	9	8	6	7	7	8	9	9.5	10	12
Operating Profit	55	7	6	7	9	7	7.3	7	8	12
Operating Margin	168.3%	20.4%	19.5%	23.5%	26.1%	19.6%	18.9%	16.7%	17.8%	22.6%
Net Profit	65	21	(3)	5	3	2	1.1	3.6	5.5	8
Net Margin	199.4%	66.9%	-8.4%	14.6%	8.7%	6.3%	2.8%	8.6%	12.2%	15.1%
Free Cash Flow	10	1	(7)	(10)	7	0	5.4	2.1	(11)	3.1
Income Tax	(17)	21	(1)	(1)	2	1	0.8	1.2	1	2.9

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	308	236	239	239	262	266	283	294	323	361
Cash & Equivalents	7	12	20	5	13	8	18	12.6	7	3.1
Accounts Receivable	1	1	1	2	1	2	2.5	2.2	2.6	3.4
Inventories	---	---	---	---	---	---	---	---	---	---
Goodwill & Int. Ass.	26	13	13	13	16	17	16	16.1	15	19.7
Total Liabilities	280	216	224	224	235	241	251	264	279	312
Accounts Payable	2	1	2	0	1	1	0.5	2.1	2.2	1
Long-Term Debt	130	104	114	114	114	114	114	113	109	108
Shareholder's Equity	28	20	15	15	28	25	32	30	44	48
LTD/E Ratio	4.69	5.19	7.62	7.70	4.11	4.64	3.56	3.75	2.45	2.21

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	---	7.9%	-1.1%	1.9%	1.2%	0.8%	---	1.3%	1.8%	2.3%
Return on Equity	---	89.5%	-14.3%	30.5%	14.5%	8.5%	---	11.6%	14.8%	17.2%
ROIC	---	15.2%	-2.0%	3.5%	2.3%	1.6%	---	2.5%	3.7%	5.2%
Shares Out.	---	---	19.1	19.6	20.5	21.5	---	22.9	23.3	24.1
Revenue/Share	1.68	1.65	1.56	1.59	1.73	1.65	---	1.83	1.92	2.20
FCF/Share	0.51	0.05	(0.35)	(0.50)	0.32	0.02	---	0.09	(0.5)	0.13

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

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