



Why Fortis Inc. Fell 12% in 1 Day and What I'm Doing About it

Description

Merger and acquisition activities usually bring down the stock price of the acquirer. Since **Fortis Inc.** ([TSX:FTS](#)) is an acquirer this morning, its shares fell as much as 12% as I'm writing this.

What's the big deal?

Fortis is planning to acquire the United States's biggest independent transmission utility, **ITC Holdings Corp.** ([NYSE:ITC](#)) for US\$11.3 billion, or US\$44.90 per share, a premium price of 14% from February 8th's closing price.

ITC owns and operates high-voltage transmission facilities in Michigan, Iowa, Minnesota, Illinois, Missouri, Kansas and Oklahoma, serving a combined peak load of over 26,000 megawatts along approximately 25,106 km of transmission line.

ITC's management team has a proven track record of operational excellence that translates to shareholder value. Since its initial public offering (IPO) in 2005, it has generated strong EPS growth, total shareholder returns, and cash flow from operations. From its IPO through to November 2015, ITC delivered more than double the annual shareholder returns of the **S&P 500 Utilities Sector Index**.

How does this acquisition affect Fortis shareholders?

Fortis expects the transaction to provide about 5% EPS accretion in the first full year following closing (excluding one-time acquisition-related expenses).

Fortis's dividend-growth guidance remains unchanged. It continues to target 6% average annual dividend growth through to 2020.

In connection with the acquisition, Fortis will apply to list its common shares on the New York Stock Exchange.

From the Fortis website: "Following the acquisition, ITC will continue as a stand-alone transmission company, retaining its focus on growth and operational excellence while benefiting from a broader

platform that will support its mission to modernize electrical infrastructure in the U.S.”

It's not a done deal yet...

The transaction is approved by the board of directors of both companies. However, it is still subject to approvals by the necessary states, shareholders, the federal government, and other regulatory bodies, such as the Federal Energy Regulatory Commission, the Committee on Foreign Investment in the United States, and the United States Federal Trade Commission/Department of Justice.

If the transaction is successful, ITC shareholders will own about 27% of the combined company.

Conclusion

Based on ITC's normal multiple, it's fully valued between US\$42.50 and US\$44 per share. From that perspective, I think Fortis paid a little premium for the ITC shares. The concern is the high foreign exchange required for converting the relatively weak Canadian dollar to the strong U.S. dollar. (Under the terms of the transaction, ITC shareholders will receive US\$22.57 in cash and 0.7520 Fortis shares per ITC share.)

However, the premiums paid for the higher share price and foreign exchange will be diluted over time as ITC starts being accretive to earnings.

Because ITC Holdings is a wide-moat business and the transaction will start to be accretive in the first full year after transaction closing, Fortis gets a “yes” vote from me. Besides, as a dividend investor, Fortis continues to target 6% average annual dividend growth, and I get the opportunity to buy more shares of this quality utility at a lower price. In fact, I just added some Fortis shares at \$36.41.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:FTS (Fortis Inc.)

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