Emera Inc. Is Unloading its Stake in Algonquin Power & Utilities Corp.

Description

On May 17, shares of **Algonquin Power & Utilities Corp.** (TSX:AQN) were halted based on major impending news. **Emera Inc.** (TSX:EMA) decided to sell 50.1 million shares in a previously negotiated deal for $10.85 per share. The deal represented roughly 20% of Algonquin Power's outstanding shares.

Before the announcement, the stock was selling at roughly $11.40 a share. While Emera continue to hold 12.9 million shares of Algonquin Power, does its sudden willingness to part with shares at a sizable discount signal that either company could be in trouble?

Management says things are fine

If you're to believe each companies' management team, the deal was simply a move to position each organization for the long term.

For Emera, that positioning includes raising capital to pay down a massive debt load it assumed during its acquisition of Florida-based **TECO Energy, Inc.** (NYSE:TE) late last year. The deal, which included $6.5 billion in cash and $3.9 billion in debt assumption, turned the company into one of the top 20 utility companies on the continent with assets going from $8 billion to $20 billion.

"Our strategic relationship with Algonquin has been and continues to be very successful for Emera," said Chris Huskilson, president and CEO of Emera. "The sale of shares was a capital allocation decision to support our proposed TECO Energy acquisition. We remain invested in [Algonquin Power] and continue to support their clean energy growth plan."

Ian Robertson, CEO of Algonquin Power, was a bit vaguer with his comments. "Algonquin's relationship with Emera has been mutually beneficial to both parties and we are pleased that it is continuing," he said, failing to reconcile that Emera chose to reduce its stake by about 80%.

A tale of two companies

While Algonquin Power has proven more than capable of compounding investor capital over the long term—shares are up over 100% in the past five years—the latest news likely bodes better for Emera considering the transformational opportunities that await the company.

While Emera was previously levered to the Canadian and northeastern U.S. markets, 56% of revenues will now come from Florida. Only 23% will stem from Canada with the remaining business spread across New England, New Mexico, and the Caribbean.

While the size and geography of Emera's business will change dramatically, the strategy that's provided years of uninterrupted dividend growth has not. Before the acquisition, 70% of the company's revenues were from regulated services, which guaranteed a certain profit margin and price increases. After the acquisition, this reliable portion of sales will actually increase to roughly 80%.

Management also anticipates plenty of room for growth in TECO's markets, which are mainly in regulatory-friendly environments. It expects the rate base (the volume of customers it serves) to grow by 5-7% annually through 2019. So even without any price increases (which are also likely), EBITDA should continue to grow at a healthy clip. These organic-growth opportunities should help management reach its long-term 8% annual dividend-growth target.

A logical choice for income investors

In all, an investment in Emera seems like a low-risk proposition. The company has grown its dividend by 8.5% annually over the last six years and has a very achievable 8% target moving forward. About 80% of its earnings are fully regulated, and falling capital expenditures should free up a considerable amount of cash flow after this year.

Following the TECO acquisition, management shouldn't have a tough time creating shareholder value over the next five years.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

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2. TSX:EMA (Emera Incorporated)

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rvanzo