How Does Altagas Ltd.'s Acquisition of WGL Holdings Inc. Benefit Shareholders?

Description

It's common for stock prices to go up or down 1-3% in a day. So, it's noteworthy if a stock rises or declines more than that in a trading session.

Altagas Ltd. (TSX:ALA) shares dipped 6.4% on Thursday. What caused the dip?

Altagas to buy WGL Holdings

Altagas is acquiring **WGL Holdings Inc.** (NYSE:WGL) for US$88.25 per share in an all-cash transaction representing an enterprise value of $8.4 billion, including the assumption of about $2.4 billion of debt.

Usually, the company that's doing the acquiring will fall in price when the announcement is made. That is the case for Altagas.

About WGL Holdings

WGL has operated for 170 years. It's a utility holding company with diversified energy-infrastructure assets, consisting of gas utilities, gas pipelines, and clean power. The company is the parent of Washington Gas, WGL Energy, WGL Midstream, and Hampshire Gas.

Washington Gas and Hampshire Gas are regulated gas utilities, which represent about 77% of WGL's assets.

In the fiscal year 2016, which ended at the end of September, Washington Gas had 1.14 million active customer metres in Virginia, Maryland, and Columbia. At the end of September, its service area had a population of about 5.7 million and included roughly 2.1 million households and commercial structures.

Hampshire Gas has interests in underground natural gas storage facilities in and around Hampshire County, West Virginia, and it operates those facilities to serve Washington Gas, which buys all of the storage services of Hampshire Gas. Washington Gas includes the cost of these services in the bills sent to its customers.

gas

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Did Altagas overpay for WGL?

Altagas is paying a price-to-earnings ratio of about 26.6 for WGL. Although on an initial look, the acquisition seems to be expensive, WGL has an above-average growth rate for a utility.

The analyst consensus is that it'd grow its earnings per share by 8% per year for the next three to five years. So, WGL could be worth the premium.

Moreover, WGL is a high-quality utility with a solid balance sheet and is awarded a high S&P credit rating of A+.

Most importantly, WGL benefits Altagas and its shareholders in multiple ways.

Benefits of the acquisition

After the acquisition, Altagas will have $22 billion of high-quality, low-risk, long-lived assets. About 75% of Altagas's earnings before interest, taxes, depreciation, and amortization will come from rate-regulated utilities and other stable earnings sources, which will improve the company's dividend durability.

The acquisition is expected to be accretive to earnings per share by 8-10% and funds from operations per share by 15-20% on average through 2021.

Additionally, it'd support an 8-10% annual dividend growth for Altagas through 2021 with a reduced payout ratio. This will be supported by $7.3 billion of organic growth capital-investment opportunities.

The takeaway

The WGL acquisition is expected to be accretive to Altagas's earnings and cash flows on a per-share basis starting in the first full year of operations. It supports Altagas's intention to grow its dividend by 8-

10% per year through 2021.

The acquisition should close by the end of Q2 2018, subject to WGL common shareholder approval and specific regulatory and government approvals.

Meanwhile, Altagas shareholders can get an above-average yield of 6.7%. If anything, income investors should consider buying the depressed shares for growing income and long-term price appreciation.

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