Altagas (TSX:ALA): This Stock Still Has Massive Upside

Description

The year 2018 was one to forget for **Altagas Ltd.** (TSX:ALA).

The company closed on its big acquisition of WGL Holdings, a Washington D.C.-based natural gas utility. Analysts almost universally agreed that Altagas paid far too much.

The deal stretched Altagas' balance sheet, which inevitably caused the dividend to be cut. The payout, which was $0.1825 per share each month, was cut to $0.08 monthly.

Shares started 2018 at close to $30 each. Investors were still optimistic about the WGL acquisition, which had been announced but hadn't closed yet. By the end of the year, the stock had lost more than 50% of its value. Altagas ended 2018 at $14 per share.

In hindsight, this turned out to be a massive buying point. Investors who got in close to the bottom — like I recommended at the time — are sitting on a gain of close to 50%.

Some might think the rally is over, but I believe this stock is just getting started. Here's why there's still 50-100% upside still left in this name.

Balance sheet is under control

Altagas has been aggressively selling non-core assets since the WGL transaction closed.

It sold its interests in various power generation projects, including this week's announcement of a $920 million sale of the power generation assets acquired from WGL.

The company also sold a mid-stream pipeline system for $379 million and it spun off some of its Canadian assets into a newly created entity, **Altagas Canada**.

Altagas pledged to sell $1.5 to $2 billion worth of assets in 2019. It has already disposed of $1.3 billion worth. All the proceeds are being applied to debt.

After peaking at more than $10 billion right after WGL closed, Altagas has done a nice job slashing debt. Total debt should be in the $7 billion range at the end of 2019.

The company's reduced dividend also ensures there's excess cash flow that can be applied to the debt. Cutting the dividend alone freed up approximately $350 million annually to put back towards debt.

Valuation

Even after rallying some 50% in 2019, Altagas shares are still quite cheap.

The company has projected it'll earn between $850 and $900 million in adjusted funds from operations (AFFO) in 2019. The stock has a market cap of $5.7 billion, putting shares at approximately 6.5 times expected AFFO. You won't find many Canadian utility stocks lower than that.

Let's compare that to **Algonquin Power and Utilities**, a similar company that is currently flirting with a 52-week high. Algonquin trades at closer to 12 times trailing AFFO. If Altagas traded at the same valuation, shares would be flirting with $40.

The stock is also cheap on a price-to-book value basis. Altagas has a price-to-book ratio of 0.91, which is much lower than its peers. Utility stocks often trade at multiples of stated book values.

Altagas traded at more than twice its book value as recently as 2014 when the stock was $50 per share.

Algonquin, by the way, trades at a little more than twice its book value today. It's very achievable for Altagas to trade at a similar valuation once it improves the balance sheet further and it starts delivering solid growth numbers.

The bottom line

Altagas is still a buy today, even after shares have moved up 50% from the lows set back in December. The stock is still significantly undervalued on both a price-to-AFFO and price-to-book value basis — and investors are collecting a generous 4.9% dividend while waiting for the price to recover.

It's not too late. You can still buy shares today and participate in this upside.

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nelsonpsmith