

Executive Summary

This report provides a comprehensive investment analysis of Xcel Energy (XEL) and Fortis Inc. (FTS), two firms in the regulated electric and gas utility industry. The analysis spans macroeconomic conditions, industry structure, ratio trends, and fundamental valuation to determine appropriate buy/hold/sell recommendations for long-term investors.

From a macroeconomic perspective, inflation is identified as a supply-side shock, raising input and capital cost while squeezing utility margins due to regulatory lag. As both firms operate in capital-intensive, regulated environments, inflation poses a meaningful threat to profit margins and valuation multiples.

The utility industry is best classified as a regulated monopoly in the maturity stage of the industry life cycle. Demand is stable and saturated across North America, with growth tied to infrastructure upgrades rather than market expansion. International exposure is minimal, and growth typically occurs through acquisitions.

Ratio trend analysis reveals XEL leads in EPS growth (5.81%) and returns to total capital (5.4%), while FTS outpaced in sales per share (4.26%) and offers a higher dividend yield (4.0% vs 3.0%). Both firms maintain manageable long-term debt and consistent dividend policies.

Fundamental analysis shows Fortis has a positive alpha (2.30%) and undervaluation across dividend models, supporting a buy recommendation. Xcel's return (8.69%) falls slightly below its required return (9.57%), producing a small negative alpha (-.88%), suggesting a hold. Sensitivity analysis confirms Fortis has more downside protection, while Xcel's higher volatility implies more valuation risk.

Insider buying and strong institutional support further reinforce Fortis's outlook, while mixed insider activity tempers enthusiasm for Xcel.

Recommendation:

Fortis Inc. (FTS): Buy- Attractive for income-focused investors seeking stability.

Xcel Energy (XEL): Hold- Fundamentally strong but better suited for growth investors willing to tolerate more risk.

Macroeconomic Analysis

This Section analyzes how inflation impacts the utility industry, focusing on Xcel Energy (XEL) and Fortis Inc. (FTS). It classifies inflation as a supply-side shock and interprets its effects on cost structures, profitability, and ultimately stock valuation. A graph illustrating the relationship between inflation and utility sector performance supports this analysis.

1.1 Inflation as a Macroeconomic Factor

Inflation remains one of the most prominent macroeconomic forces shaping corporate performance in 2025. In the U.S., the Consumer Price Index (CPI) has increased approximately 2.4% year-over-year, while Canada reports inflation at 2.3% (BLS, 2025; StatCan, 2025). Utility companies are particularly exposed to inflation because of their reliance on long-term infrastructure projects, fuel procurement, and labor-intensive operations. For firms like Xcel Energy (XEL) and Fortis Inc. (FTS), inflation leads to increased construction costs, higher prices for equipment and materials, and elevated wage pressures across operations.

Notably, these companies operate in regulated environments where pricing power is limited in the short term. This regulatory lag prevents immediate rate adjustments, meaning cost increases often squeeze margins. According to Value Line, Fortis is already experiencing this effect, with the report noting that “high inflation and supply-chain constraints” are negatively impacting the bottom line. While utilities often benefit from stable demand due to the essential nature of their services, inflation’s erosion of purchasing power and increased cost of capital introduce meaningful downside risk for investors.

1.2 Classification as Supply Shock

Inflation qualifies as a supply-side shock for XEL and FTS because it primarily impacts the cost of inputs rather than demand for electricity or gas. Utility services are typically price-inelastic consumers do not significantly reduce consumption in response to moderate price increases, so inflation does not directly suppress revenue. However, inflation increases the cost of raw materials (e.g., copper, steel), skilled labor, and energy inputs like natural gas. These costs increase compress profit margins and reduce free cash flow.

In addition, inflation raises financing costs. As central banks raise interest rates to combat inflation, utilities must pay more to issue debt, which is a major funding source for capital intensive infrastructure projects. This raises the weighted average cost of capital (WACC), lowering the net present value of future cash flows and making new investments less attractive.

In this way, inflation indirectly reduces future growth opportunities, reinforcing its role as a negative supply shock.

Table 1: Inflation vs Utility Sector Performance



Table 1 illustrated above plots the year-over-year U.S inflation rate, alongside the utilities Select sector SPDR Fund (XLU), a proxy for utility sector performance (BLS,2025; Yahoo Finance,2025). The graph demonstrates that periods of elevated inflation (e.g., 2022-2023) coincide with weaker utility returns, indicating the sector's vulnerability to rising input costs and interest rates. This pattern supports the classification of inflation as a supply-side shock with meaningful implications for stock performance.

1.3 Interpretation

Inflation poses a significant supply-side threat to the utility industry by increasing the cost of inputs like fuel, copper, and labor, pressuring margins for capital-intensive firms such as Xcel Energy and Fortis Inc. This pressure is intensified by rising interest rates, which raise borrowing costs and reduce investment efficiency. Though utilities benefit from stable demand, their long-term debt and regulatory lag make them vulnerable in inflationary environments. As shown in Table 1, utilities outperformed briefly during the 2022 inflation spike (8.5%), but performance declined sharply as costs caught up, demonstrated by XLU's -9.1% return in 2023. Ultimately, rising costs reduce future cash flows and valuations, especially for firms with long planning horizons and rate-setting delays like XEL and FTS.

1.4 Conclusion

Inflation functions as a supply-side shock in the utility industry by increasing the cost of inputs and capital while limiting immediate pricing power due to regulatory constraints. This has clear negative implications for Xcel Energy and Fortis Inc., whose profitability is sensitive to labor, infrastructure, and energy costs. While eventual rate relief may partially offset these pressures, the timing and magnitude of such adjustments remain uncertain. As a result, the utility sector is likely to underperform the broader market if inflation remains elevated or accelerates further. Investors should remain cautious in the near term, particularly when evaluating dividend sustainability and growth potential amid compressed margins.

2. Industry Analysis

Xcel Energy (XEL) and Fortis Inc. (FTS) operate within the regulated electric and gas utility industry, providing essential infrastructure and energy services to residential, commercial, and industrial customers. The industry is characterized by stable demand, high capital intensity, and significant regulatory oversight. These characteristics make it relatively defensive, though utility firms remain vulnerable to macroeconomic shocks, regulatory shifts, and infrastructure risks.

2.1 Market Structure

Xcel Energy (XEL) and Fortis Inc. (FTS) operate in a regulated monopoly structure, where high infrastructure costs prevent competition, and firms are granted exclusive regional rights under strict regulatory oversight (FERC, 2024). While utilities provide commoditized services like electricity and gas, they may differentiate through reliability or sustainability efforts. Despite monopoly status, pricing power is limited, as rates must be approved through lengthy regulatory processes, often lagging behind rising input costs. However, participation in regional transmission organizations (RTOs) and access to market-based rate mechanisms allow limited flexibility to manage short-term volatility, helping offset the fiscal impact of regulatory delays.

2.2 Industry Life Cycle

The utility industry, including firms like Xcel Energy (XEL) and Fortis Inc. (FTS), is firmly in the maturity stage of its life cycle. Demand is stable and price inelastic, with nearly full market saturation across North America. Growth is slow, driven by population trends rather than innovation or competition. Strict regulatory oversight further limits pricing flexibility and expansion speed but enhances financial stability. The industry now emphasizes infrastructure upgrades and grid modernization over market expansion, with capital investments focused on

efficiency and environmental goals. Both XEL and FTS follow dividend-focused models, reflecting the sector's appeal to income-focused, risk-averse investors.

2.3 Role of International Markets

The utility industry primarily operates in saturated markets across North America. In both the U.S and Canada, electricity and natural gas services are considered essential infrastructure, and nearly all residential and commercial areas already have access. As a result, there are very few untapped or unsaturated markets within these countries. Any meaningful customer growth tends to occur incrementally through population growth or new construction, not from market expansion. Therefore, for firms like Fortis Inc. and Xcel Energy, expansion opportunities in non-saturated markets are limited domestically and typically require international acquisitions to gain access to new service territories.

With regard to imports and exports, utility firms do not rely heavily on cross-border trade for their core goods or services. Electricity and gas are typically generated and consumed locally due to the logistical and financial inefficiencies of long-distance transmission. While there may be some regional grid interconnections that allow for occasional energy transfers between jurisdictions, such as between U.S and Canada, these exchanges are situational and supplementary, not central to the firms' operating models.

In summary, the utility industry does not depend on international trade for core revenues, and growth through unsaturated markets is rare. Expansion beyond existing territories usually occurs through regulated acquisitions rather than organic entry into underdeveloped regions.

2.4 Five-year trend Ratio Analysis

2.4.1 Sales Per Share

Sales	XEL	FTS
2024	23.40	23.19
2023	25.60	23.48
2022	27.86	22.90
2021	24.69	19.90
2020	21.45	19.14
2019	21.98	18.96
Trend	1.77%	4.26%

From 2019 to 2024, Fortis Inc. (FTS) grew sales per share at an average rate of 4.26%, outpacing Xcel Energy (XEL) by 1.77%. This suggests stronger revenue growth or tighter share count control by Fortis. Xcel's slower growth may reflect more frequent share issuance or modest revenue expansion, a common tradeoff in capital-intensive industries like utilities.

2.4.2 Earnings Per Share

EPS	XEL	FTS
2024	3.50	3.28
2023	3.35	3.10
2022	3.17	2.78
2021	2.96	2.61
2020	2.79	2.60
2019	2.64	2.68
Trend	5.81%	4.25%

From 2019 to 2024, Xcel Energy (XEL) posted stronger EPS growth (5.81%) than Fortis. Inc (FTS) (4.25%), signaling superior earnings momentum. Xcel's edge likely reflects better cost control or regulatory outcomes, while Fortis's steady growth points to consistent performance, possibly tempered by exchange rates or regulatory lags. Both firms show resilient profitability, but XEL in per-share earnings strength.

2.4.3 Net Profit Margin

NPM	XEL	FTS
2024	15.0%	14.1%
2023	13.1%	13.1%
2022	11.4%	12.1%
2021	12.0%	13.1%
2020	13.0%	13.6%
Average	12.9%	13.2%

Over the past five years, Fortis Inc. (FTS) maintained a slightly higher average net profit margin (13.2%) than Xcel Energy (XEL) (12.9%). Both firms operate with relatively stable margins, reflecting the predictable nature of regulated utility revenues. Fortis's consistency may stem from smoother regulatory frameworks or cost structures, while Xcel's recent NPM uptick to 15% in 2024 suggests improving operational efficiency or rate adjustments.

2.4.4 Return on Total Capital (ROA)

ROTC	XEL	FTS
2024	5.5%	4.7%
2023	5.4%	4.5%
2022	5.5%	2.4%
2021	5.3%	4.2%
2020	5.4%	4.3%
Average	5.4%	4.0%

Between 2020 and 2024, Xcel Energy (XEL) posted a stronger average return on total capital (5.4%) compared to Fortis Inc. (FTS) (4.0%). This suggests XEL has been more effective at generating returns from its total invested capital, reflecting better asset utilization or project performance. Fortis's dip in 2022 may indicate capital tied up in less immediately productive assets or slower regulatory recovery on investments. Overall, XEL appears more efficient in converting capital into profits.

2.4.5 Long Term Debt

LTD (in Mils)	XEL	FTS
2024	28,243	31,614
2023	26,013	27,613
2022	23,915	26,301
2021	22,994	24,072
2020	21,062	23,477
2019	19,033	21,990
Trend	8.24%	7.61%

From 2019 to 2024, Xcel Energy's (XEL) long-term debt increased at an average annual rate of 8.24%, slightly outpacing Fortis Inc. (FTS) at 7.61%. This steady rise reflects the capital-intensive nature of the utility sector, where debt is often used to finance large-scale infrastructure and grid modernization. While both firms rely heavily on debt to fund growth, XEL's higher rate suggests more aggressive expansion or refinancing. Elevated LTD levels are typical in regulated utilities but underscore the importance of managing interest rate exposure and maintaining favorable credit ratings.

2.4.6 P/E Ratio

P/E	XEL	FTS
2024	17.0	17.3
2023	19.0	18.0
2022	22.2	21.1
2021	22.5	21.2
2020	23.9	20.6
Average	20.9	19.6

Over the 2020-2024 period, Xcel Energy (XEL) traded at an average P/E ratio of 20.9, slightly higher than Fortis Inc. (FTS) at 19.6. This suggests that investors have historically been willing

to pay a modest premium for XEL's earnings, potentially reflecting stronger EPS growth or greater confidence in future performance. Both companies' P/E ratios have trended downward in recent years, likely due to rising interest rates compressing valuation multiple across the utility sector. Despite the decline, the averages remain in line with long-term sector norms, reflecting the steady, income-focused nature of regulated utilities.

2.4.7 Dividend Yield

Div Yld	XEL	FTS
2024	3.7%	4.0%
2023	3.3%	4.3%
2022	2.8%	4.1%
2021	2.8%	3.8%
2020	2.6%	3.7%
Average	3.0%	4.0%

From 2020 to 2024, Fortis Inc. (FTS) consistently offered higher dividend yields than Xcel Energy (XEL), averaging 4.0% versus XEL's 3.0%. This reflects Fortis's emphasis on shareholder income, which aligns with its appeal to conservative, income-oriented investors. XEL, while still maintaining reliable dividends, appears to balance income returns with reinvestment for growth. Fortis's higher yield may also reflect slightly lower valuation multiples, while XEL's relatively lower yield suggests the market anticipates stronger capital appreciation. Overall, both firms remain attractive to dividend-focused investors, but FTS has the edge in yield consistency and payout level.

2.4.8 Payout Ratio

Payout	XEL	FTS
2024	60.0%	82.0%
2023	59.0%	81.0%
2022	58.0%	78.0%
2021	59.0%	52.0%
2020	58.0%	67.0%
Average	58.8%	72.0%

Fortis Inc. (FTS) has averaged a higher payout ratio (72%) than Xcel Energy (XEL) at 58.8%, reflecting a stronger focus on returning earnings to shareholders. This supports Fortis's income-oriented strategy but may limit reinvestment flexibility. Xcel's lower payout indicates a more balanced approach, retaining capital to fund growth while still offering stable dividends.

2.5 Conclusion

Based on the five-year trend analysis, both Xcel Energy (XEL) and Fortis Inc. (FTS) demonstrate solid financial foundations, but with different strengths. Xcel shows stronger earnings growth (EPS) at a year-over-year growth rate of 5.81% reflecting stronger earnings momentum, supported by efficient capital use and steady operational performance, as seen in its superior return on total capital (5.4%). Its modest 3.0% dividend yield and consistent $\approx 59\%$ payout ratio suggest a balanced strategy of reinvestment and shareholder returns.

Fortis, meanwhile, leads in sales per share growth at 4.26% and offers a higher 4.0% average dividend yield with a more generous 72% payout ratio. This positions FTS well for income-oriented investors but may limit reinvestment capacity. Its profitability and return on capital remain healthy, though slightly behind Xcel, suggesting slower but stable performance.

Long-term debt growth for both firms, 8.24% for Xcel and 7.61% for Fortis, is manageable and expected given the capital-intensive nature of utilities. Valuation multiples, as reflected by

average P/E ratios, are comparable, though Xcel's recent compression suggests either a more cautious market outlook or a potential buying opportunity.

In summary, both firms are financially sound, with Xcel leaning toward long-term growth and Fortis delivering consistent income. Investors seeking dividend stability may favor FTS, while those prioritizing earnings growth and capital efficiency may find XEL more compelling. These insights support a "hold" or "buy" stance on both stocks, depending on individual investment goals.

3. Fundamental Analysis

3.1 CAPM

Fortis Inc. (FTS)		Xcel Energy (XEL)	
Current Price	62.7400	Current Price	67.0600
Current Risk-free Rate	0.0432	Current Risk-free Rate	0.0432
# of Years	3.0000	# of Years	3.0000
Beta	0.7500	Beta	0.7500
Historical Risk-free	0.0400	Historical Risk-free	0.0400
Historical Market Return	0.1100	Historical Market Return	0.1100
Historical Equity Premium	0.0700	Historical Equity Premium	0.0700
CAPM		CAPM	
Required Rate of Return:	9.57%	Required Rate of Return:	9.57%

The 9.57% represents the minimum annual return investors should demand for holding XEL or FTS, given their risk profile relative to the overall market. A stock delivering a return higher than this threshold would be considered to generate positive risk-adjusted performance (Alpha). If the expected or actual return is lower, the stock underperforms relative to its risk.

CAPM serves as a benchmark for comparing other valuation models and return expectations. It's particularly important for utility companies like XEL and FTS, whose lower beta values reflect the relative stability and lower volatility of the sector.

3.2 Expected Holding Period Return

Fortis Inc. (FTS)	Xcel Energy (XEL)
Expected HPR	
3-Year Expected HPR:	40.00%
Annual Expected HPR:	11.87%
	Undervalued
Alpha	
Alpha:	2.30%
	Undervalued
Alpha	
Alpha:	-0.88%
	Overvalued

Over the 3-year holding period, Fortis Inc. (FTS) is expected to deliver a total return of 40.00%, translating to an annualized return of 11.87%, which exceeds its CAPM-based required rate of return of 9.57%. This positive spread results in an alpha of 2.30%, suggesting that Fortis is undervalued and may offer returns above what is required for its level of risk.

In contrast, Xcel Energy (XEL) has a projected 3-year return of 28.39%, or an annualized return of 8.69%, which is below its required rate of return. This yields a negative alpha of -.088%, indicating overvaluation relative to expected risk-adjusted returns.

This comparison supports a buy recommendation for Fortis due to its positive alpha, and a more cautious stance on Xcel, suggesting a hold or reevaluation.

3.3 Dividends

Fortis Inc. (FTS)

Xcel Energy (XEL)

Future Dividend Yield Model		Future Dividend Yield Model	
Estimated Future Price =	\$75.45	Estimated Future Price =	\$75.31
Present Value (Intrinsic Value) =	\$57.36	Present Value (Intrinsic Value) =	\$57.25
Overvalued		Overvalued	
Dividend Discount Model		Dividend Discount Model	
Intrinsic Value:	\$26.37	Intrinsic Value:	\$24.30
	Overvalued		Overvalued
Gordon Growth Model		Gordon Growth Model	
Intrinsic Value:	\$63.57	Intrinsic Value:	\$68.39
	Undervalued		Undervalued

Dividends play a key role in valuing Fortis and Xcel due to their stable payout histories. The Future Dividend Yield Model values Fortis at \$57.36 and Xcel at \$57.25, both below current prices, suggesting overvaluation. The Dividend Discount Model estimates even lower intrinsic values: \$26.37 for Fortis and \$24.30 for Xcel. In contrast, the Gordon Growth Model, which assumes growing dividends, shows Fortis valued at \$63.57 and Xcel at \$68.39, implying both are slightly undervalued. Given their history of consistent dividend growth, the GGM provides the most reliable estimate, reinforcing their appeal to long-term, income-focused investors.

3.4 Sensitivity Analysis

Fortis Inc. (FTS)

Sensitivity Analysis

If P/E is:	If EPS is:				
	20% less	10% less	As expected	10% more	20% more
20% less	-1.974%	1.437%	4.633%	7.645%	10.497%
10% less	1.437%	5.019%	8.372%	11.530%	14.518%
As expected	4.633%	8.372%	11.870%	15.161%	18.275%
10% more	7.645%	11.530%	15.161%	18.577%	21.807%
20% more	10.497%	14.518%	18.275%	21.807%	25.145%

Xcel Energy (XEL)

Sensitivity Analysis					
<i>If P/E is:</i>	<i>If EPS is:</i>				
	20% less	10% less	As expected	10% more	20% more
	20% less	-4.847%	-1.510%	1.615%	4.560%
	10% less	-1.510%	1.993%	5.270%	8.355%
	As expected	1.615%	5.270%	8.688%	11.902%
	10% more	4.560%	8.355%	11.902%	15.238%
	20% more	7.347%	11.274%	14.942%	18.390%

Sensitivity Analysis was conducted to measure how changes in EPS and P/E assumptions affect each stock's expected return. Fortis (FTS) demonstrated more stability: its worst-case scenario (20% drop in both EPS and P/E) still yields a modest -1.97% return, while its best-case scenario projects a gain of 25.15%. This narrower downside reflects greater resilience to earnings or valuation volatility.

Xcel (XEL), on the other hand, showed wider sensitivity. Its worst-case scenario results in a steeper decline of -4.85%, while the best-case outcome is a return of 21.65%. This suggests that Xcel's stock price is more reactive to forecast deviations, especially on the downside.

For both firms, upside returns improve significantly with increases in either EPS or P/E. However, due to Fortis's milder downside and stronger baseline assumptions, it may be more suitable for conservative investors. Xcel, while offering strong upside, may carry more valuation risk. Based on this, Fortis is a buy in most moderate to strong scenarios, while Xcel is a buy primarily under bullish assumptions.

3.5 Insiders and Institutional Investors

According to the Canadian Insider, in February 2025, CEO of Fortis Inc. (FTS), David Hutchens purchased 12,000 shares at approximately \$43.78 per share, signaling confidence in the company's prospects (Fortis Inc., 2025). Institutional investors hold about 52.7% of Fortis's shares, indicating strong institutional backing.

As for Xcel, the Nasdaq reports show that institutional ownership stands at approximately 84.43%, reflecting significant institutional interest, (Nasdaq, 2025). It has also been reported that Director Devin Stockfish acquired 2,170 shares at \$68.93 per share in March 2025, while other executives have sold shares in the past year.

The insider buying at Fortis suggests a positive outlook from a company leadership, supporting a buy recommendation. For Xcel Energy, mixed insider activity and high institutional ownership suggest a more cautious approach, aligning with a hold recommendation.

3.6 Conclusion on Fundamental Valuation

Fundamental analysis shows that Fortis Inc. (FTS) is slightly undervalued, supported by a positive alpha (2.30%), strong dividend valuation under the Gordon Growth Model, and stable performance in sensitivity testing. Insider buying and solid institutional support further reinforce a buy recommendation, especially for income-focused investors.

Xcel Energy (XEL), while financially sound, appears slightly overvalued with a negative alpha (-.88%) and higher downside sensitivity. Its valuation models are mixed, and insider activity is less consistent. As a result, XEL is best categorized as a hold, offering long-term potential but with greater valuation risk in the near term.

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