Badger Meter (BMI)

Updated October 17th, 2018 by Nate Parsh

Key Metrics

Current Price:	$50	**5 Year CAGR Estimate:**	0.0%	**Volatility Percentile:**	63.4%
Fair Value Price:	$39	**5 Year Growth Estimate:**	3.4%	**Momentum Percentile:**	66.9%
% Fair Value:	128%	**5 Year Valuation Multiple Estimate:**	-4.6%	**Growth Percentile:**	17.5%
Dividend Yield:	1.2%	**5 Year Price Target**	$47	**Valuation Percentile:**	17.2%
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Total Return Percentile:**	4.2%

Overview & Current Events

Badger Meter was founded in 1905 in Milwaukee, WI. The company's first product was a "frost proof" water meter. Today, Badger Meter manufactures and markets meters and valves that are used to measure and control the flow of liquids, such as water, oil and various chemicals. The company's products are also used to control the flow of air and other gases. Badger Meter has a market cap of $1.25 billion and generated more than $400 million in sales in 2017. The company is also a founding member of the American Water Works Association, a trade group that sets water measurement standards in the U.S.

Badger Meter reported 3rd quarter earnings on October 17th. The company earned a 3rd quarter record of $0.46 per share, beating estimates by $0.05 and improving more than 70% year over year. Revenue grew 10.6% to $110.63 million while also topping estimates by $0.96 million.

Sales to municipalities increased 16% year over year and represented 78% of total sales. Badger Meter's E-Series Ultrasonic water meters and ORION Cellular endpoints were a source of strength during the quarter. As in previous quarters, international sales were strong, with management once again highlighting their business in the Middle East. BMI increased the prices for its products in January and these increases contributed 4% to revenue growth during the quarter. Higher volume sales help Badger Meter's gross margins grow to nearly 40%, up 3% from the prior year. SG&A climbed 14% to $28.12, with much of the increase related to executive compensation.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$0.85	$0.90	$0.96	$0.64	$0.98	$0.85	$1.03	$0.90	$1.11	$1.19	***$1.65***	***$1.95***
DPS	$0.20	$0.23	$0.26	$0.30	$0.33	$0.35	$0.37	$0.39	$0.43	$0.49	***$0.60***	***$1.01***
Shares	29.62	29.95	30.10	30.25	28.63	28.82	28.92	29.05	29.12	29.12	***28.5***	***28.0***

Badger Meter has increased earnings per share by 3.4% per year over the past decade. We expect the company to earn $1.65 per share in 2018, thanks in large part to a much lower tax rate. Investors should note that Badger Meter does not offer quarterly guidance.

Badger Meter has increased its dividend for the past 26 years. The company has increased its dividend by an average of 11% per year over the past 10 years. BMI raised its dividend 15.4% on 8/1/2018. Dividend growth has varied over the past few years, with 15% raise in 2016 and ~5% raises in 2015 and 2014.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	24.9	19.8	21	28	18.9	28.8	25.6	33.2	30.6	34.8	***30.3***	***23.9***
Avg. Yld.	0.9%	1.3%	1.3%	1.7%	1.8%	1.4%	1.4%	1.3%	1.3%	1.1%	***1.1%***	***2.1%***

Shares of Badger Meter have been at their most expensive over the past three years. As these years could be outliers, they were not included in the 2023 multiple estimate. Shares of Badger Meter have increased in price by $3, or 6.4%, since our July 19th update, offering a forward multiple of 30.3. This is well above the 2008-2014 average P/E of 23.9. If the stock was to revert to this average, shares would have a multiple contraction of 4.6% per year through 2023.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Badger Meter has rewarded shareholders with low double digit dividend growth over the past decade, but that still equates to a very low dividend yield (currently 1.2%).

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	50.4%	50.8%	47.6%	41%	42.1%	37%	38.4%	38.2%	43.1%	39.8%	***40.4%***	***42.8%***
Debt/A	43.2%	24.4%	22%	18.1%	41%	37.8%	37.2%	34.7%	26.7%	29.2%	***29.6%***	***31.4%***
Int. Cov.	246.6	469.4	309.2	148.9	92.3	35.6	40.6	34.8	55.1	70.5	***65.9***	***47.3***
Payout	23.5%	25.6%	28.9%	46.9%	33.7%	41.2%	36%	43.3%	38.7%	41.2%	***36.4%***	***51.8%***
Std. Dev.	88.8%	59.8%	31.3%	42.2%	34.5%	31.1%	25.2%	24%	27%	26.4%	***28.9%***	***26.7%***

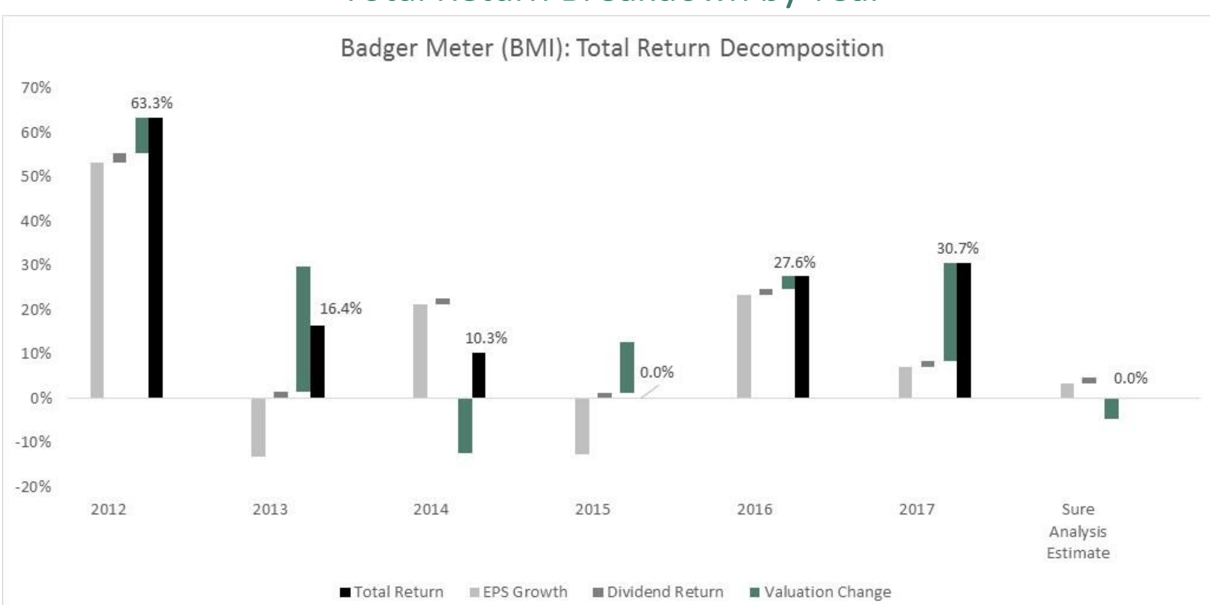
Unlike many companies at the height of the last recession, earnings for Badger Meter actually improved. The vast majority of the company's sales are made to municipal water utilities. Consumers still need access to water, even in a recession. It is estimated that there are more than 30 million water meters in the U.S. that are not monitored with the advanced equipment that BMI offers. And with some states, like California, looking to improve its water monitoring systems in times of droughts, BMI is in a prime position to benefit.

Badger Meter has seen its gross-profit-to-assets ratio decline from the 50% range, but this metric has stabilized in the past few years. Tax reform will be a major benefit to the company in future years, which should allow profitability to increase. Badger Meter has also seen debt as a percentage of assets decline to nearly a 10 year low. Badger Meter maintains a very low payout ratio, even in years in which earnings declined (2011, 2013 and 2015). Because of the company's low payout ratio and above-average dividend history, Badger Meter earns a C rating for Dividend Safety, although its low yield causes it to earn an F rating for Retirement Suitability.

Final Thoughts & Recommendation

After the increase in share price, we now estimate that Badger Meter will offer 0% annualized returns, down from our prior estimate of 1%. While 26 years of dividend growth is impressive for this small company, we feel that there are much better places for investors to invest their capital. The company earns a sell recommendation at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	279.6	250.3	276.6	262.9	319.7	334.1	364.8	377.7	393.8	402.4
Gross Profit	98.5	97.0	102.8	89.8	122.2	117.0	131.1	135.8	150.6	155.7
Gross Margin	35.2%	38.8%	37.2%	34.2%	38.2%	35.0%	36.0%	35.9%	38.2%	38.7%
SG&A Exp.	57.6	54.8	58.0	62.3	77.8	77.9	85.1	93.4	99.8	100.1
D&A Exp.	7.1	8.2	8.5	9.5	12.1	13.5	15.7	20.6	22.4	24.4
Operating Profit	40.9	42.2	44.8	27.5	44.5	39.1	46.0	42.4	50.8	55.6
Operating Margin	14.6%	16.9%	16.2%	10.5%	13.9%	11.7%	12.6%	11.2%	12.9%	13.8%
Net Profit	25.1	34.2	28.7	19.2	28.0	24.6	29.7	25.9	32.3	34.6
Net Margin	9.0%	13.6%	10.4%	7.3%	8.8%	7.4%	8.1%	6.9%	8.2%	8.6%
Free Cash Flow	-12.7	28.8	1.1	26.0	26.6	20.5	23.4	16.1	45.6	34.7
Income Tax	14.5	15.6	15.8	8.2	15.4	13.4	15.2	15.2	17.5	20.3

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	195.4	191.0	215.9	218.9	290.5	316.1	341.2	355.5	349.7	391.7
Cash & Equivalents	6.2	13.3	3.1	5.0	6.6	7.3	6.7	8.2	7.3	11.2
Accounts Receivable	N/A	N/A	N/A	N/A	N/A	N/A	54.0	56.6	59.8	58.2
Inventories	39.3	32.5	48.3	49.4	61.0	60.9	71.8	78.6	77.7	85.2
Goodwill & Int. Ass.	32.0	30.6	43.3	43.0	94.3	102.0	109.4	105.3	101.2	126.8
Total Liabilities	84.3	46.6	47.5	39.6	119.2	119.5	126.8	123.2	93.5	114.3
Accounts Payable	13.2	10.8	11.2	11.4	15.6	18.6	16.1	19.2	18.4	28.6
Long-Term Debt	25.2	8.0	12.9	1.8	66.7	70.0	75.9	71.4	38.0	44.6
Shareholder's Equity	111.0	144.5	168.4	179.3	171.2	196.6	214.3	232.3	256.2	277.5
D/E Ratio	0.2	0.1	0.1	0.0	0.4	0.4	0.4	0.3	0.1	0.2

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	14.5%	17.7%	14.1%	8.8%	11.0%	8.1%	9.0%	7.4%	9.2%	9.3%
Return on Equity	24.7%	26.7%	18.3%	11.0%	16.0%	13.4%	14.4%	11.6%	13.2%	13.0%
ROIC	20.5%	23.7%	17.2%	10.6%	13.4%	9.8%	10.7%	8.7%	10.8%	11.2%
Shares Out.	29.62	29.95	30.10	30.25	28.63	28.82	28.92	29.05	29.12	29.12
Revenue/Share	9.42	8.37	9.22	8.74	11.10	11.57	12.68	13.07	13.55	13.82
FCF/Share	-0.43	0.96	0.04	0.86	0.92	0.71	0.81	0.56	1.57	1.19

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.