Badger Meter (BMI)

Updated April 19th, 2019 by Nathan Parsh

Key Metrics

Current Price:	$56	**5 Year CAGR Estimate:**	-1.6%	**Volatility Percentile:**	64.3%
Fair Value Price:	$41	**5 Year Growth Estimate:**	3.4%	**Momentum Percentile:**	93.2%
% Fair Value:	137%	**5 Year Valuation Multiple Estimate:**	-6.1%	**Growth Percentile:**	19.2%
Dividend Yield:	1.1%	**5 Year Price Target**	$48	**Valuation Percentile:**	11.6%
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Total Return Percentile:**	3.0%

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 capitalization of $1.6 billion and generates more than $450 million in annual revenues. 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 released financial results for the first quarter on 4/17/2019. The company earned $0.37 per share, $0.01 above estimates and a 42% increase from the previous year. Revenue declined slightly to $105 million, which was $6.2 million below estimates.

Municipal water sales improved 1% despite extreme weather in the first quarter of the year negatively impacting quarterly results. Customers also deferred orders while waiting for Badger Meter's E-Series Ultrasonic water meters and ORION Cellular products to ramp up production. The demand for these products has been high in previous quarters. Flow instrumentation products were down 3% because of foreign currency exchange. Operating margins improved 420 bps to 13.7% while gross profit margins increased 360 bps to 38.6%. The improvement in gross margins, due to sales mix and lowered costs, is impressive given that sales were essentially flat year-over-year. Expenses declined 60 bps. We expect the company to earn $1.71 per share in 2019, up from $1.68 previously.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$0.90	$0.96	$0.64	$0.98	$0.85	$1.03	$0.90	$1.11	$1.19	$1.54	***$1.71***	***$2.02***
DPS	$0.23	$0.26	$0.30	$0.33	$0.35	$0.37	$0.39	$0.43	$0.49	$0.56	***$0.60***	***$0.94***
Shares	30	30	30	29	29	29	29	29	29	29	***29***	***29***

Badger Meter has increased earnings per share by 3.4% per year over the past decade. The company's products showed strong growth last year and we continue to see earnings-per-share growing due to this demand of at least 3.4% per year through 2024. Badger Meter's ability to control costs, and thereby boost margins, should help offset any weakness in revenue that may occur.

Badger Meter has increased its dividend for the past 26 years. The company has increased its dividend by an average of 9.3% per year over the past 10 years. Dividend growth has varied over the past few years, with a 15% raise in 2016 following ~5% raises in 2015 and 2014. Badger Meter raised its dividend 15.4% on 8/1/2018.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	19.8	21.0	28.0	18.9	28.8	25.6	33.2	30.6	34.8	30.3	***32.7***	***23.9***
Avg. Yld.	1.3%	1.3%	1.7%	1.8%	1.4%	1.4%	1.3%	1.3%	1.1%	1.1%	***1.1%***	***1.9%***

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Shares of Badger Meter have been at their most expensive valuations over the past three years. As these years could be outliers, they were not included in the 2024 multiple estimate. Shares of Badger Meter have decreased by $3, or 5.1%, since our February 10th update. Using estimates for earnings-per-share for 2019, the stock has a current multiple of 32.7. This is well above the 2008-2014 average price-to-earnings ratio of 23.9. If the stock were to revert to this average, shares could see annual returns reduced by 6.1% per year through 2024.

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 today (currently 1.1%). We see a declining valuation as the catalyst for the yield to rise closer to 2% over time from the current 1.1%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	26%	29%	47%	34%	41%	36%	43%	39%	41%	36%	***35%***	***47%***

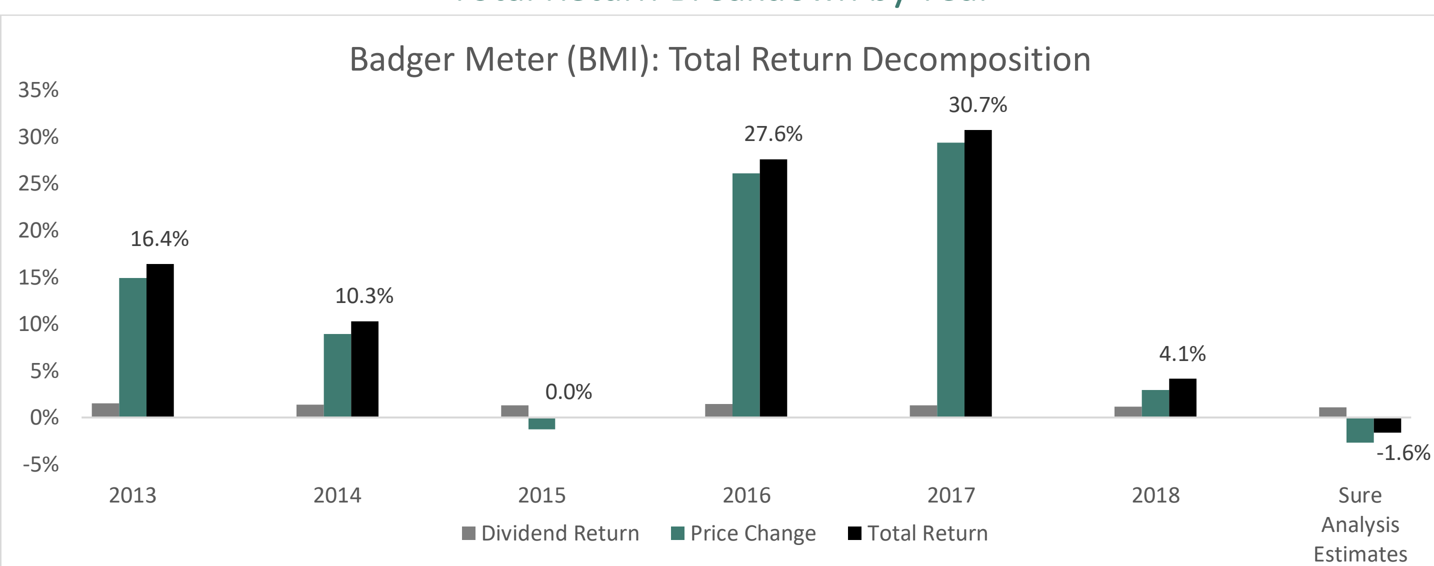
Given Badger Meter's 26-year dividend increase streak and low payout ratio, the dividend is very safe today. We also see plenty of room for growth in the payout, so Badger Meter is certainly attractive from a dividend growth perspective.

Unlike many companies at the height of the last recession, earnings-per-share for Badger Meter actually improved. The vast majority of the company's sales are made to municipal water utilities. A key competitive advantage that Badger Meter possess is that consumers will still need access to water in a recession. In addition, 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 Badger Meter offers. And with some states like California looking to improve its water monitoring systems for use in times of droughts, the company is in a prime position to benefit from upgrades and improvements.

Final Thoughts & Recommendation

After reviewing first quarter results, we estimate that shares of Badger Meter are likely to lose 1.6% annually through 2024, an improvement from our previous estimate of a 3% loss. Badger Meter's expensive valuation is more appropriate for high growth companies, not those offering low single digit earnings growth. The low yield and low earnings growth rates, collectively, are more than offset by the valuation that is currently 137% of fair value. We maintain our sell rating on the stock and our 2024 price target of $48.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	250	277	263	320	334	365	378	394	402	434
Gross Profit	97	103	90	122	117	131	136	151	156	162
Gross Margin	38.8%	37.2%	34.2%	38.2%	35.0%	36.0%	35.9%	38.2%	38.7%	37.4%
SG&A Exp.	55	58	62	78	78	85	93	98	99	105
D&A Exp.	8	8	9	12	13	16	21	22	24	24
Operating Profit	42	45	28	44	39	46	42	53	57	57
Operating Margin	16.9%	16.2%	10.5%	13.9%	11.7%	12.6%	11.2%	13.4%	14.1%	13.1%
Net Profit	34	29	19	28	25	30	26	32	35	28
Net Margin	13.6%	10.4%	7.3%	8.8%	7.4%	8.1%	6.9%	8.2%	8.6%	6.4%
Free Cash Flow	29	1	26	27	21	23	16	46	35	52
Income Tax	16	16	8	15	13	15	15	18	20	8

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	191	216	219	290	316	341	355	350	392	393
Cash & Equivalents	13	3	5	7	7	7	8	7	11	13
Accounts Receivable	N/A	N/A	41	46	50	54	57	60	58	66
Inventories	32	48	49	61	61	72	79	78	85	81
Goodwill & Int. Ass.	31	43	43	94	105	114	105	101	133	132
Total Liabilities	47	47	40	119	119	127	123	93	114	89
Accounts Payable	11	11	11	16	19	16	19	18	29	22
Long-Term Debt	8	13	2	67	70	76	71	38	45	18
Shareholder's Equity	144	168	179	171	197	214	232	256	277	304
D/E Ratio	0.06	0.08	0.01	0.39	0.36	0.35	0.31	0.15	0.16	0.06

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	17.7%	14.1%	8.8%	11.0%	8.1%	9.0%	7.4%	9.2%	9.3%	7.1%
Return on Equity	26.7%	18.3%	11.0%	16.0%	13.4%	14.4%	11.6%	13.2%	13.0%	9.6%
ROIC	23.7%	17.2%	10.6%	13.4%	9.8%	10.7%	8.7%	10.8%	11.2%	8.6%
Shares Out.	30	30	30	29	29	29	29	29	29	29
Revenue/Share	8.37	9.22	8.74	11.10	11.57	12.68	13.07	13.55	13.82	14.86
FCF/Share	0.96	0.04	0.86	0.92	0.71	0.81	0.56	1.57	1.19	1.77

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