



Artesian Resources Corp. (ARTNA)

Updated June 30th, 2019 by Lyn Alden

Key Metrics

Current Price:	\$37	5 Year CAGR Estimate:	3.2%	Volatility Percentile:	59.6%
Fair Value Price:	\$32	5 Year Growth Estimate:	3.5%	Momentum Percentile:	31.2%
% Fair Value:	117%	5 Year Valuation Multiple Estimate:	-3.0%	Growth Percentile:	21.1%
Dividend Yield:	2.7%	5 Year Price Target	\$38	Valuation Percentile:	34.7%
Dividend Risk Score:	C	Retirement Suitability Score:	C	Total Return Percentile:	19.7%

Overview & Current Events

Artesian Resources Corporation (ARTNA) was founded in 1905 in New Castle County, Delaware. Through its subsidiaries, the company provides water, wastewater and other services primarily in the Delaware region. Artesian Resources sells and distributes water to residential, commercial, industrial, governmental, and utility customers throughout the state. In addition, Artesian Resources provides water for public and private fire protection in Delaware, Maryland, and Pennsylvania. The company produces 7.9 billion gallons of water annually through 1,311 miles of water main with a population of approximately 301,000 served. Artesian has 241 employees, a market capitalization of over \$340 million, and generated more than \$80 million in revenue in 2018.

On May 8, 2019, Artesian Resources reported first quarter results for the period ended March 31, 2019. Revenue for the quarter was \$19.4 million, a 2.5% increase compared to the first quarter of 2018. Earnings per share were \$0.39, a 5.4% increase compared to the same period last year. The CEO did not provide guidance, but noted that she expects that the company's infrastructure investments in 2018 should provide a strong foundation of growth for 2019.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$0.97	\$1.00	\$0.83	\$1.13	\$0.94	\$1.07	\$1.26	\$1.41	\$1.51	\$1.54	\$1.59	\$1.89
DPS	\$0.72	\$0.75	\$0.76	\$0.79	\$0.82	\$0.85	\$0.87	\$0.90	\$0.93	\$0.96	\$0.98	\$1.16
Shares	7.45	7.65	8.61	8.71	8.83	8.91	9.06	9.13	9.22	9.25	9.30	9.65

Artesian Resources has enjoyed strong growth for a utility. EPS growth over the past 10 years has averaged 5.1% per year, 5-year EPS growth has averaged over 8.2% per year, and 3-year EPS growth has averaged just under 4.1% per year. Growth has been decelerating lately, and we expect 3.5% growth over the next five years. Delaware's population growth averages approximately 1% per year, which along with 2% annual price increases, provides a baseline growth rate for the company of approximately 3.0%. The company can potentially increase this further by offering new services or expanding its area, but growth beyond 4.0% per year may be difficult going forward.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	16.8	18.2	22.5	18.3	23.9	20.5	18.0	20.9	24.2	23.9	23.3	20.0
Avg. Yld.	4.4%	4.1%	4.1%	3.8%	3.7%	3.9%	3.8%	3.1%	2.5%	2.6%	2.7%	3.0%

Due to its stability, Artesian Resources has historically commanded a rather high valuation. Its P/E ratio dropped to under 17 during the previous recession but has often floated over 20 during normal economic times. Currently the P/E ratio is higher than 23 and its dividend yield is under 2.7%, below its historical norm.

Low government bond yields across the developed world have resulted in substantial equity premiums for recession-resistant stocks, meaning that even at rich valuations they potentially offer a strong return premium over safe government bonds. Still, we believe that paying over 20x annual earnings is too rich, and that a P/E of 20 or less for a company with this level of growth and high earnings resiliency is warranted.

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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Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	74.2%	75%	91.6%	69.9%	87.2%	79.4%	69.0%	63.8%	61.6%	62.3%	61.6%	61.4%

Artesian Resources earned approximately \$14.2 million in net income during the past year, and has long-term debt of slightly over \$115 million. This equates to a debt/income ratio of over 8x. Debt/EBIT is approximately 4.8x. Annual interest expense is approximately 25% of operating income, meaning that the company has an interest coverage ratio of approximately 4x. The company uses a substantial amount of leverage, but is in line with other utilities on this metric due to their stable cash flows and large base of assets.

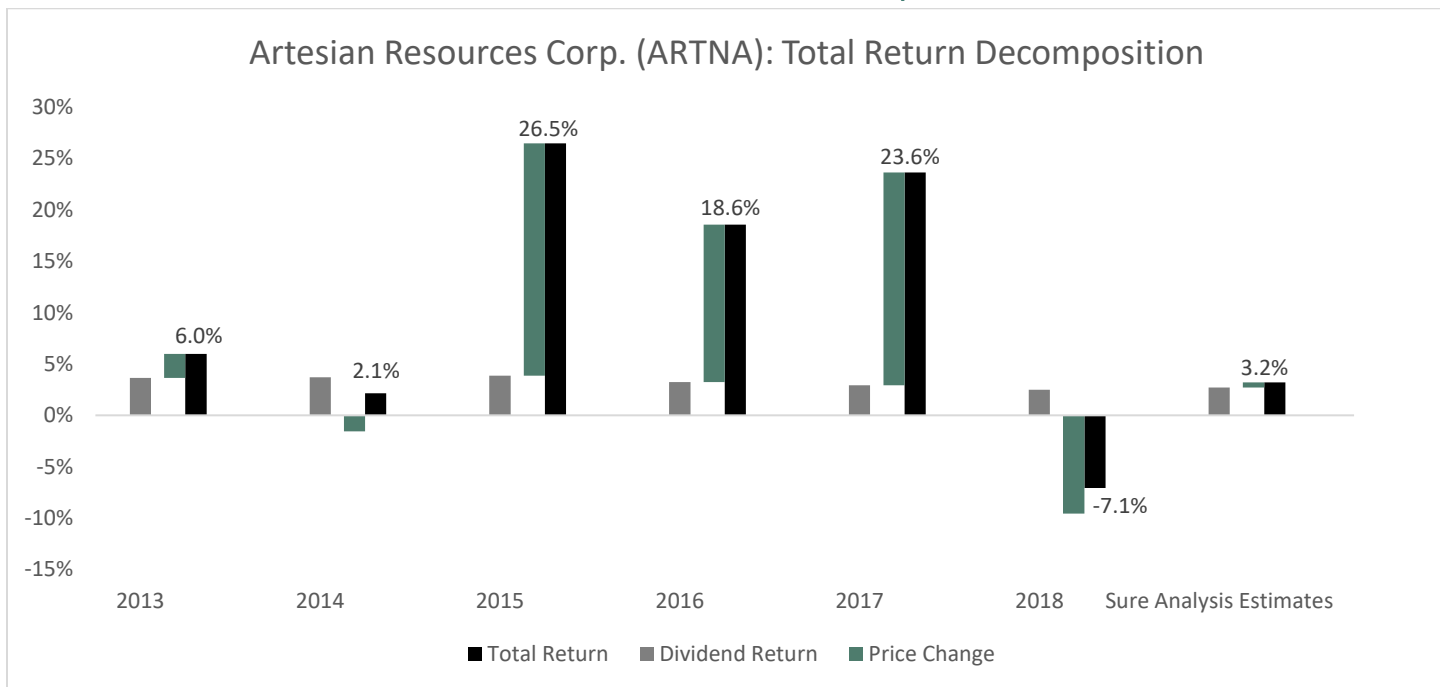
Like most utilities, the company's earnings have historically been very recession-resistant. During the previous recession, their earnings-per-share declined by 5% in 2007 and declined by a further 7% in 2008. By 2009, the company had recovered to match its 2006 peak earnings, and surpassed that peak in 2010. The company operates in a regulated environment with long-term contracts, and its cash flows should be very safe going forward. The company has increased its dividend for 27 consecutive years, although at times the payout ratio became high. Since 1992, the company has had the same CEO, Dian Taylor, who has proven to be an intelligent allocator of shareholder capital.

Final Thoughts & Recommendation

Artesian Resources has been a very successful utility company with a long stretch of consecutive annual dividend increases, and a solid growth rate in an otherwise slow-growing industry.

However, valuations have become very high in the utility sector, and Artesian Resources has not been spared from this. Forward returns are likely to be lower than past returns, as the company's P/E multiple is above its long-term average and its dividend yield is below its long-term average. We expect total returns over the next five years to average approximately 3.2% per year, and therefore consider Artesian Resources to be a sell at the current time.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	61	65	65	71	69	72	77	79	82	80
Gross Profit	29	30	30	34	32	35	39	41	41	39
Gross Margin	46.9%	46.5%	45.5%	48.7%	47.0%	48.8%	50.1%	51.6%	50.1%	48.8%
D&A Exp.	7	7	7	8	8	9	9	9	10	10
Operating Profit	14	20	19	23	20	23	26	27	27	25
Operating Margin	22.4%	30.1%	28.5%	32.3%	29.5%	31.4%	33.3%	34.6%	33.1%	30.6%
Net Profit	7	8	7	10	8	10	11	13	14	14
Net Margin	11.9%	11.7%	10.4%	14.0%	12.0%	13.1%	14.7%	16.4%	17.0%	17.8%
Free Cash Flow	-4	-2	3	3	0	-5	8	2	-5	-20
Income Tax		5	5	7	6	6	8	8	7	5

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	359	372	379	392	404	422	432	451	495	530
Cash & Equivalents	0	0	0	1	0	0	0	0	1	0
Accounts Receivable	6	5	3	4	4	4	5	5	5	6
Inventories	1	1	1	1	1	2	2	2	2	1
Total Liabilities	268	276	266	274	282	297	299	312	348	377
Accounts Payable	4	3	3	3	4	4	5	6	9	8
Long-Term Debt	133	136	120	118	117	125	115	111	117	134
Shareholder's Equity	91	95	113	118	122	126	132	139	147	153
D/E Ratio	1.46	1.43	1.06	1.00	0.96	0.99	0.87	0.80	0.79	0.87

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	2.1%	2.1%	1.8%	2.6%	2.1%	2.3%	2.6%	2.9%	3.0%	2.8%
Return on Equity	8.1%	8.2%	6.5%	8.5%	6.9%	7.7%	8.8%	9.5%	9.8%	9.5%
ROIC	3.3%	3.4%	2.9%	4.2%	3.5%	3.9%	4.5%	5.2%	5.5%	5.2%
Shares Out.	7.51	7.62	8.16	8.72	8.84	8.93	9.01	9.16	9.24	9.29
Revenue/Share	8.11	8.52	7.97	8.09	7.82	8.12	8.55	8.63	8.90	8.65
FCF/Share	-0.53	-0.20	0.42	0.32	-0.02	-0.59	0.86	0.17	-0.58	-2.14

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

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