# Artesian Resources Corp. (ARTNA)

*Updated October 5th, 2019 by Lyn Alden*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $37 | **5 Year CAGR Estimate:** | 3.2% | **Volatility Percentile:** | 49.3% |
| **Fair Value Price:** | $32 | **5 Year Growth Estimate:** | 3.5% | **Momentum Percentile:** | 50.5% |
| **% Fair Value:** | 116% | **5 Year Valuation Multiple Estimate:** | -3.0% | **Growth Percentile:** | 25.5% |
| **Dividend Yield:** | 2.6% | **5 Year Price Target** | $38 | **Valuation Percentile:** | 34.8% |
| **Dividend Risk Score:** | C | **Retirement Suitability Score:** | D | **Total Return Percentile:** | 19.6% |

## Overview & Current Events

Artesian Resources Corp. (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. Artesiasn has 241 employees, a market capitalization of over $340 million, and generated more than $80 million in revenue in 2018.

On August 7, 2019, Artesian Resources reported second quarter results for the period ended June 30, 2019. Revenue for the quarter was $20.7 million, a 2.0% increase compared to the second quarter of 2018. Earnings per share were $0.41, which is down from $0.42 from last year. The CEO did not provide guidance, but noted that the company is completing major infrastructure investments this year.

## 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**[1] | 7.5 | 7.7 | 8.6 | 8.7 | 8.8 | 8.9 | 9.1 | 9.1 | 9.2 | 9.3 | ***9.3*** | ***9.7*** |

Artesian Resources has enjoyed strong growth for a utility. EPS growth over the past 9 years has averaged 5.3% per year and 5-year EPS growth has averaged over 8.2% per year.

Growth has been decelerating in the past four years, 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%. The company can potentially increase this further by offering new services or expanding its area, but growth beyond 4% 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% | ***2.6%*** | ***3.1%*** |

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 2.6%, 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 sizable return premium over safe

[1] Share count is in millions.

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.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2024 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Payout** | 74% | 75% | 92% | 70% | 87% | 79% | 69% | 64% | 62% | 62% | ***62%*** | ***62%*** |

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 less than 5x. 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.

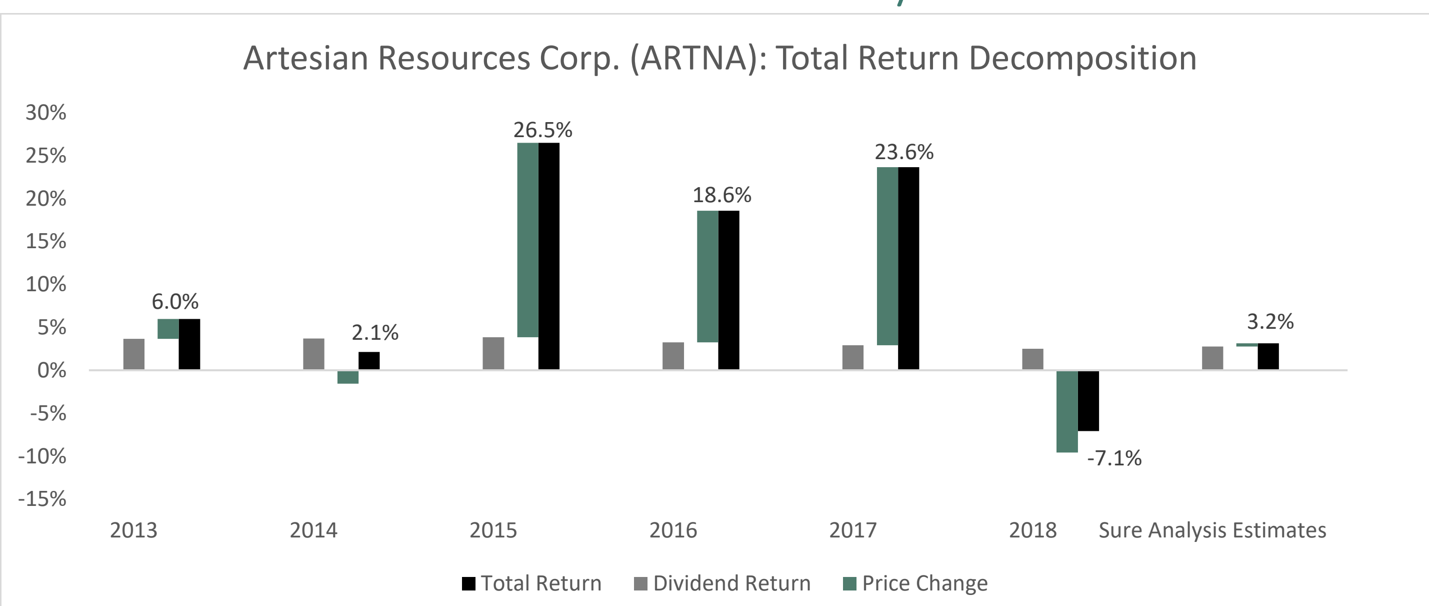
Like most utilities, the company's earnings have historically been very recession resistant. During the previous recession, the company's earnings-per-share declined by 5% in 2007 and declined by a further 7% in 2008. By 2009, the company had recovered to match its 2006 peak earnings and surpassed that 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 was 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.*