



Artesian Resources Corp. (ARTNA)

Updated January 8th, 2020 by Samuel Smith

Key Metrics

Current Price:	\$37	5 Year CAGR Estimate:	3.2%	Market Cap:	\$339M
Fair Value Price:	\$32	5 Year Growth Estimate:	3.5%	Ex-Dividend Date:	2/7/2020 ¹
% Fair Value:	116%	5 Year Valuation Multiple Estimate:	-3.0%	Dividend Payment Date:	2/22/2020 ²
Dividend Yield:	2.6%	5 Year Price Target	\$38	Years Of Dividend Growth:	21
Dividend Risk Score:	C	Retirement Suitability Score:	D	Last Dividend Increase:	3%

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. Artesian has 241 employees, a market capitalization of \$339 million, and generated more than \$80 million in revenue in 2018.

On November 6, 2019, Artesian Resources reported third quarter results for the period ended September 30, 2019. Net income grew by 13.5% year-over-year and diluted earnings-per-share increased by 14.3% year-over-year to \$0.48. Revenues also grew, but at a considerably slower pace (2.9%) than net income. Some of the main reasons for the more rapid growth in profits was because revenues outgrew operating expenses (2.5%), and an 18.3% decline in income taxes.

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
Shares³	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. Earnings-per-share growth over the past 9 years has averaged 5.3% annually, and 5-year earnings-per-share growth has averaged 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.

¹ Estimate

² Estimate

³ Share count is in millions.

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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 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 stable cash flows and large base of assets.

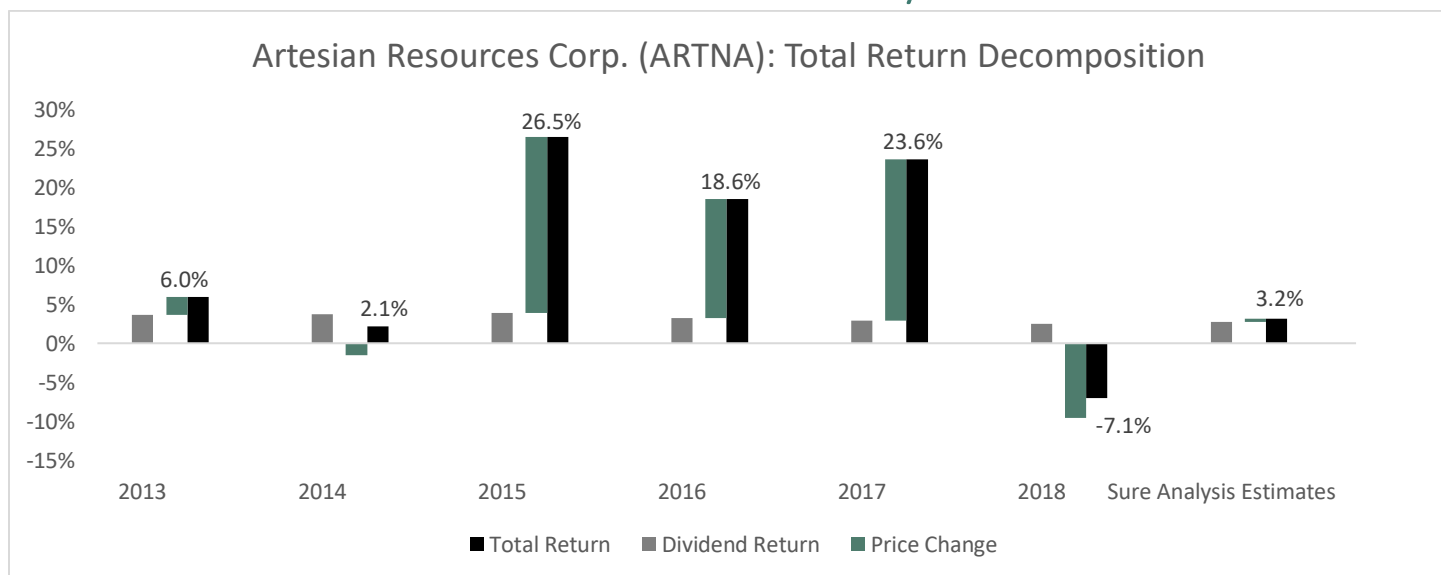
Like most utilities, the company's earnings have historically been very recession resistant. During the previous recession, the company's earnings-per-share declined by 5% in 2007 and declined by a further 7% in 2008. By 2009, the company had recovered to match its 2006 peak earnings and surpassed that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

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