



Black Hills Corporation (BKH)

Updated November 11th, 2020 by Jonathan Weber

Key Metrics

| | | | | | |
|-----------------------------|------|--|------|----------------------------------|----------|
| Current Price: | \$64 | 5 Year CAGR Estimate: | 7.8% | Market Cap: | \$4.0B |
| Fair Value Price: | \$66 | 5 Year Growth Estimate: | 4.0% | Ex-Dividend Date: | 11/16/20 |
| % Fair Value: | 97% | 5 Year Valuation Multiple Estimate: | 0.5% | Dividend Payment Date: | 12/01/20 |
| Dividend Yield: | 3.5% | 5 Year Price Target | \$80 | Years Of Dividend Growth: | 49 |
| Dividend Risk Score: | A | Retirement Suitability Score: | A | Last Dividend Increase: | 5.6% |

Overview & Current Events

Black Hills Corporation is an electric utility that provides electricity and natural gas to customers in Colorado, Iowa, Kansas, Montana, Nebraska, South Dakota, and Wyoming. Black Hills was founded in 1941, and the company is headquartered in Rapid City, South Dakota. Black Hills Corporation has increased its dividend for 49 years in a row, which qualifies it as a Dividend Champion, and a potential Dividend King in just 1 year.

Black Hills Corporation reported its third quarter earnings results on November 2. The company generated revenues of \$350 million during the quarter, which was 7% more than the revenues that Black Hills Corporation was able to generate during the previous year's quarter. Black Hills Corporation's revenues were a lot lower than what the analyst community had expected, missing the consensus estimate by \$52 million, or well above 10%.

Black Hills Corporation generated earnings-per-share of \$0.58 during the third quarter, which was easily higher than the consensus analyst estimate of \$0.50. Earnings-per-share were up by \$0.14 versus the previous year's quarter, showcasing the resilience of the company's results during the current crisis. Q2 and Q3 are seasonally weaker quarters due to lower natural gas demand, but management believes that earnings-per-share will come in at ~\$3.65 this year, which would represent a small increase in its profits versus fiscal 2019.

Growth on a Per-Share Basis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$1.66 | \$1.01 | \$1.97 | \$2.61 | \$2.89 | \$2.83 | \$3.13 | \$3.36 | \$3.54 | \$3.53 | \$3.65 | \$4.44 |
| DPS | \$1.44 | \$1.46 | \$1.48 | \$1.52 | \$1.56 | \$1.62 | \$1.68 | \$1.81 | \$1.93 | \$2.05 | \$2.26 | \$2.88 |
| Shares¹ | 39 | 44 | 44 | 45 | 45 | 51 | 53 | 54 | 58 | 61 | 63 | 65 |

Black Hills' profitability has been rather volatile over the last decade. Overall, earnings-per-share have grown by 5% annually in the 2009 to 2019 time frame. This is not a bad growth rate for a utility, as utilities seldom grow their profits at a high pace. Black Hills' earnings-per-share growth rate was relatively consistent, except for 2011.

The swings in Black Hills' profits are primarily based on the impact that weather conditions have on the demand for electricity, for cooling in summer, and natural gas, for heating in winter. Black Hills' growth over the coming years depends on several factors. This includes rate reviews, which drive revenues and profits per kWh. Another factor is the expansion of the company's existing assets via new utility infrastructure. Black Hills regularly adds new projects to its growth investment backlog, which currently stands at \$2.7 billion for the 2020-2024 time frame. Black Hills' planned growth investments include new electric transmission lines and new natural gas pipelines to service its customers.

Rate reviews will allow Black Hills to recover investments into its existing systems, thereby more or less guaranteeing increasing revenues, which should lead to rising profits down the road. In 2018, Black Hills exited its oil business, which means that the company is now less impacted by changes in commodity prices. Focusing on its core utility business will likely be a positive for Black Hills going forward. We forecast a mid-single digit earnings-per-share growth rate in the long run, but there will likely be some ups and downs due to the impact of weather in specific quarters.

¹ In Millions

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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Valuation Analysis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | Now | 2025 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | 18.1 | 31.1 | 17.1 | 18.2 | 19.0 | 16.1 | 22.3 | 19.7 | 17.8 | 22.4 | 17.5 | 18.0 |
| Avg. Yld. | 4.8% | 4.6% | 4.4% | 3.2% | 2.8% | 3.5% | 2.9% | 2.7% | 3.3% | 2.6% | 3.5% | 3.6% |

Black Hills Corporation trades for close to 18 times this year’s expected net profits at current prices. Black Hills’ valuation has moved in a very wide range throughout the past. The company was valued at less than 10 times profits during the midst of the financial crisis, but at as much as 30 times earnings in 2011. Shares trade below our fair value estimate right now, but only to a very small degree, which is why multiple expansion will not be a major tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|--------|-------|------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Payout | 86.7% | 145% | 75.1% | 58.2% | 54.0% | 57.2% | 53.7% | 53.9% | 54.5% | 58.1% | 61.9% | 65.0% |

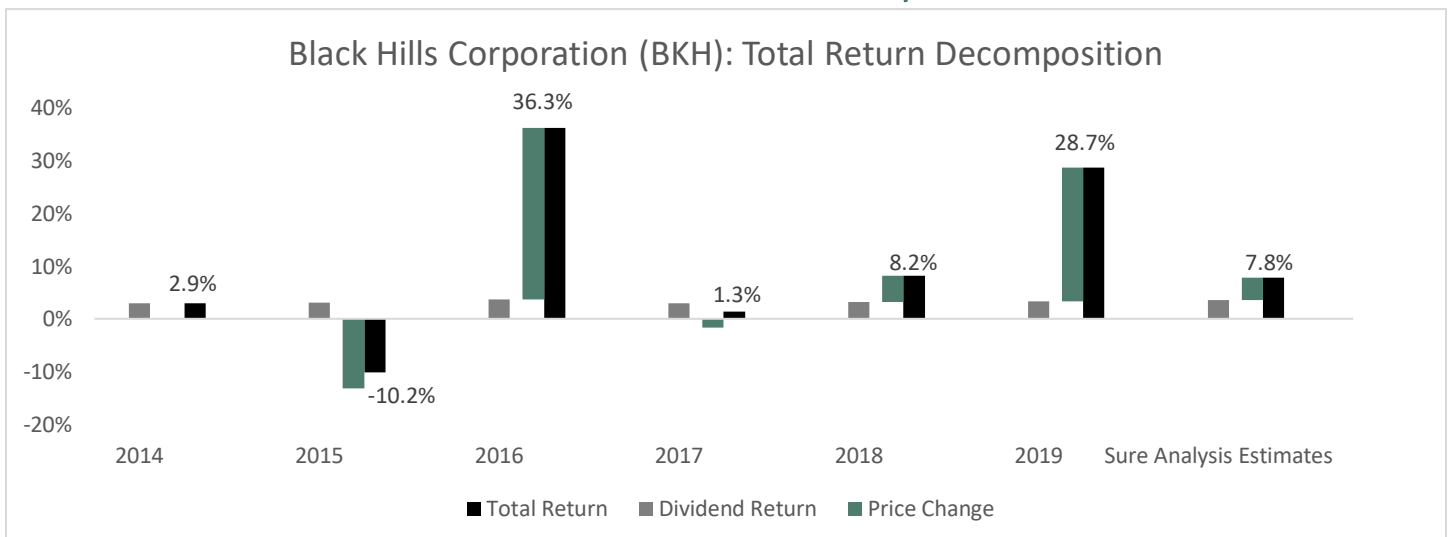
Overall, Black Hills Corporation’s dividend payout ratio declined between 2010 and 2019, due to a modest dividend growth rate. Today, the company pays out roughly 60% of its net profits in the form of dividends. It should be noted that Black Hills Corporation was not able to cover its dividend with net profits during 2008, when profits took a hit. The same thing happened during 2011. The company nevertheless raised its dividend during those years, and its decades-long dividend growth track record gives investors assurance that a dividend cut is unlikely from this utility company.

Demand for electricity and gas is not overly cyclical, although it is dependent upon weather conditions to some degree. Thus, Black Hills should remain profitable under most circumstances. The fact that customers tend to stick with their provider means that Black Hills operates a relatively stable business model. The company should also be able to weather future recessions well, which creates appeal for more conservative investors.

Final Thoughts & Recommendation

Black Hills is a relatively small utility company, but it has a compelling dividend growth track record, having raised its dividend annually for almost five decades in a row. We believe that it is highly likely that the company will continue to grow its earnings and its dividend over the coming years. The company’s shares trade close to our fair value estimate right now; we do not forecast major multiple changes. We rate the stock a hold at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | 1,220 | 1,272 | 1,174 | 1,276 | 1,394 | 1,261 | 1,539 | 1,680 | 1,754 | 1,735 |
| Gross Profit | 653 | 356 | 439 | 438 | 453 | 481 | 613 | 662 | 647 | 668 |
| Gross Margin | 53.5% | 28.0% | 37.4% | 34.3% | 32.5% | 38.1% | 39.8% | 39.4% | 36.9% | 38.5% |
| Operating Profit | 183 | 186 | 250 | 259 | 264 | 300 | 336 | 417 | 397 | 406 |
| Operating Margin | 15.0% | 14.6% | 21.3% | 20.3% | 18.9% | 23.8% | 21.8% | 24.8% | 22.6% | 23.4% |
| Net Profit | 69 | 50 | 102 | 117 | 131 | (32) | 73 | 177 | 258 | 199 |
| Net Margin | 5.6% | 3.9% | 8.7% | 9.2% | 9.4% | -2.5% | 4.7% | 10.5% | 14.7% | 11.5% |
| Free Cash Flow | (325) | (217) | (32) | (30) | (83) | 158 | (134) | 102 | 31 | (313) |
| Income Tax | 22 | 18 | 60 | 63 | 67 | 79 | 59 | 73 | (24) | 30 |

Balance Sheet Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Total Assets | 3,712 | 4,127 | 3,729 | 3,838 | 4,246 | 4,627 | 6,542 | 6,659 | 6,963 | 7,558 |
| Cash & Equivalents | 16 | 22 | 15 | 8 | 21 | 441 | 14 | 15 | 21 | 10 |
| Accounts Receivable | 172 | 98 | 101 | 114 | 119 | 80 | 137 | 126 | 147 | 145 |
| Inventories | 63 | 84 | 78 | 88 | 91 | 87 | 104 | 113 | 117 | 117 |
| Goodwill & Int. Ass. | 357 | 357 | 357 | 357 | 357 | 363 | 1,308 | 1,307 | 1,314 | 1,313 |
| Total Liabilities | 2,611 | 2,918 | 2,497 | 2,554 | 2,892 | 3,161 | 4,812 | 4,839 | 4,676 | 5,094 |
| Accounts Payable | 147 | 105 | 84 | 130 | 124 | 90 | 152 | 161 | 211 | 194 |
| Long-Term Debt | 1,440 | 1,628 | 1,320 | 1,479 | 1,618 | 1,930 | 3,314 | 3,326 | 3,142 | 3,495 |
| Shareholder's Equity | 1,100 | 1,209 | 1,233 | 1,284 | 1,354 | 1,466 | 1,615 | 1,709 | 2,182 | 2,362 |
| D/E Ratio | 1.31 | 1.35 | 1.07 | 1.15 | 1.19 | 1.32 | 2.05 | 1.95 | 1.44 | 1.48 |

Profitability & Per Share Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|--------|--------|--------|--------|--------|-------|--------|-------|-------|--------|
| Return on Assets | 2.0% | 1.3% | 2.6% | 3.1% | 3.2% | -0.7% | 1.3% | 2.7% | 3.8% | 2.7% |
| Return on Equity | 6.3% | 4.3% | 8.4% | 9.3% | 9.9% | -2.3% | 4.7% | 10.7% | 13.3% | 8.8% |
| ROIC | 2.8% | 1.8% | 3.8% | 4.4% | 4.6% | -1.0% | 1.7% | 3.5% | 4.9% | 3.5% |
| Shares Out. | 39 | 44 | 44 | 45 | 45 | 51 | 53 | 54 | 58 | 61 |
| Revenue/Share | 31.20 | 31.74 | 26.64 | 28.72 | 31.25 | 27.85 | 28.89 | 30.48 | 31.62 | 28.54 |
| FCF/Share | (8.30) | (5.41) | (0.73) | (0.68) | (1.87) | 3.49 | (2.52) | 1.86 | 0.56 | (5.15) |

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

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