Mueller Water Products, Inc. (MWA)

Updated May 16th, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	$11.65	**5 Year CAGR Estimate:**	1.9%	**Market Cap:**	$1.82 B
Fair Value Price:	$9.00	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	05/09/2022
% Fair Value:	129%	**5 Year Valuation Multiple Estimate:**	-5.0%	**Dividend Payment Date:**	05/20/2022
Dividend Yield:	2.0%	**5 Year Price Target**	$11.49	**Years Of Dividend Growth:**	8
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Rating:**	Sell

Overview & Current Events

Mueller Water Products is a leading manufacturer and marketer of products and services used to transmit, distribute, and measure water in North America. The company's products and services are used by municipalities and the residential and non-residential construction industries. The majority of its revenues (>90%) are derived from spending on water and wastewater infrastructure upgrades, repairs, and replacements, typically associated with the construction of new residential communities. Management estimates it has one of the largest installed bases of Iron Gate valves and fire hydrants in the United States. The company generates around $1.1 billion in annual sales and is based in Atlanta, Georgia.

On May 2nd, 2022, Mueller Water Products reported its Q2-2022 results for the period ending March 31st, 2022. For the quarter, revenues came in at $310.5 million, 16.1% higher year-over-year. The increase in revenues was primarily due to higher pricing across most of its product lines and increased volumes. Water Flow Solutions was the segment that contributed the most to this growth, with its sales rising 25% to $183.9 million. The Water Management Solutions segment also performed well, growing sales by 5.1% to $126.6 million, driven by the same catalysts as well as the addition of i2O Water, which the company acquired last summer.

Net income per diluted share came in at $0.15 as compared with $0.13 last year, with lower interest expenses partly offsetting the 6.5% increase in operating expenses.

For the FY-2022, Mueller now anticipates that consolidated net sales will increase between 10% and 12% (previously 6% to 10%) as compared with the prior year. These expectations take into account the current backlog, higher pricing, new product initiatives, and channel strategies. Despite a guidance upgrade on sales, we continue to expect FY2022 EPS at $0.50 due to rising costs leading to compressed profit margins.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	($0.69)	$0.26	$0.35	$0.19	$0.40	$0.77	$0.67	$0.40	$0.45	$0.44	***$0.50***	***$0.64***
DPS	$0.07	$0.07	$0.07	$0.08	$0.10	$0.15	$0.19	$0.20	$0.21	$0.22	***$0.23***	***$0.28***
Shares[1]	156.5	157.7	159.2	160.5	161.3	160.1	158.2	157.8	157.8	158.4	***156.9***	***150.0***

Despite Mueller's revenue modestly growing over the past few years, they are still near the same levels they were a decade ago. The company has sustained a positive bottom line since 2013, but with no growth success, nonetheless. Its industry is very mature, with little to no expansion prospects. Hence apart from acquisitions, the company has few growth avenues. Further, the currently accelerated inflation could hurt the company if it isn't able to match higher costs with adequate price increases.

Still, powered by growing revenues, we estimate EPS growth of 5% in the medium-term. Mueller has never cut its dividend since its IPO. It has grown annually over the past 7 years, though at a humble rate since 2018. We expect DPS

[1] Share count is 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.

growth of around 4% going forward, considering Mueller's limited profitability growth catalysts ahead. The company repurchased another $20 million worth of stock in Q2. Continuous buybacks should contribute to EPS growth.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	---	29.8	26.1	48.5	29.7	15.6	17.2	26.2	22.5	48.0	***23.3***	***18.0***
Avg. Yld.	2.0%	0.9%	0.8%	0.9%	0.8%	1.3%	1.7%	1.9%	2.0%	1.5%	***2.0%***	***2.5%***

Over the past decade, Mueller's valuation multiple has hovered to various levels based on the company's profitability expectations. Shares are currently trading at 23.3 times our expected FY2022 EPS. Despite the recent sales rebound, due to its overall lagged financials, we believe that shares would be more fairly valued at a lower multiple of around 18. A lower multiple is even further justified in a rising rates environment, with the company's thin growth prospects hardly deserving a premium. The only catalyst behind the stock's current premium, in our view, lies in all water-related investments attracting significant investor interest due to their mature and mission-critical business models. We expect the stock's yield to move up, assuming a reasonable valuation compression, though it is to remain rather soft overall.

Safety, Quality, Competitive Advantage, & Recession Resiliency

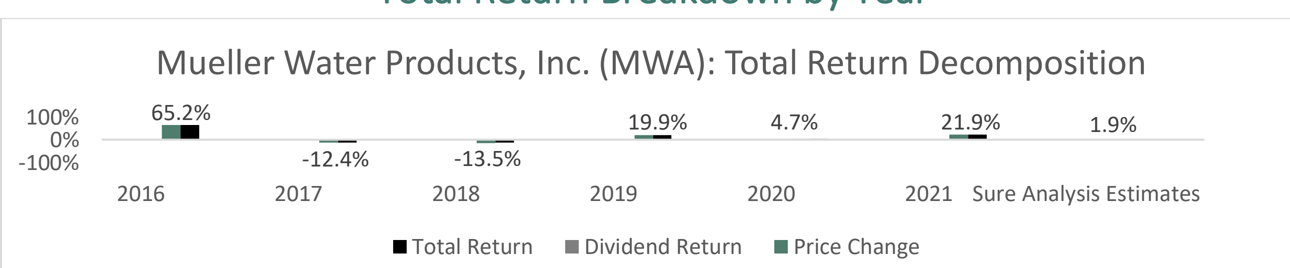
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	---	27%	20%	42%	25%	19%	28%	50%	46%	50%	***46%***	***44%***

We consider the stock's dividend relatively safe even as the payout ratio has moved higher over the past few years. The company is a market leader in water and wastewater infrastructure upgrades that see relatively stable annual demand. Water utility companies must modernize their facilities every a certain time period; hence robust demand should remain. The company claims that while the valve and hydrant products industry is competitive, it is a mature one and many end users are slow to transition to brands other than their historically preferred brand. Hence sales should not fluctuate wildly. Sales should remain relatively stable under a recession as well, as was the case during the Great Financial Crisis. However, the company still has little to no competitive advantages and is subject to limited growth catalysts ahead. On the positive side, Mueller's net debt position has been declining consistently, from $1.5 billion in 2006 to $283 million as of the latest quarter. The company also has no outstanding debt maturities prior to June 2029, which should allow for flexible capital allocation in the medium-term.

Final Thoughts & Recommendation

Mueller Water Products possesses certain attractive qualities, such as robust revenues, an improving balance sheet, and a healthy dividend payout ratio. However, we forecast the stock will deliver insignificant returns in the coming years due to potentially strong valuation reversion headwinds ahead, which could offset gains from growth in the company's financials and yield. We believe there are better plays in water-related stocks. Consequently, we rate shares a sell at their current levels.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	1,121	1,185	793	801	826	916	968	964	1111
Gross Profit	313	348	246	269	268	290	321	328	359
Gross Margin	27.9%	29.4%	31.0%	33.6%	32.4%	31.6%	33.2%	34.0%	32.3%
SG&A Exp.	214	221	147	150	155	167	183	198	219
D&A Exp.	59	57	43	40	42	44	53	58	60
Operating Profit	99	124	80	112	102	113	122	117	140
Operating Margin	8.8%	10.5%	10.0%	14.0%	12.4%	12.3%	12.6%	12.1%	12.6%
Net Profit	41	56	31	64	123	106	64	72	70
Net Margin	3.6%	4.7%	3.9%	8.0%	14.9%	11.5%	6.6%	7.5%	6.3%
Free Cash Flow	73	111	61	114	(25)	77	6	73	94
Income Tax	9	18	8	24	24	(10)	18	22	25

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	1,282	1,313	1,230	1,281	1,258	1,292	1,337	1,395	1,518
Cash & Equivalents	124	161	113	195	362	347	177	209	228
Accounts Receivable	165	182	175	132	145	164	173	181	212
Inventories	209	198	219	131	139	157	191	163	185
Goodwill & Int. Ass.	553	534	507	435	439	420	529	509	508
Total Liabilities	954	961	862	861	769	727	745	754	823
Accounts Payable	101	116	99	74	83	90	85	67	92
Long-Term Debt	601	541	489	484	481	445	446	448	447
Shareholder's Equity	328	350	366	418	488	563	590	641	695
LTD/E Ratio	1.83	1.55	1.34	1.16	0.98	0.79	0.76	0.70	0.64

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	3.2%	4.3%	2.4%	5.1%	9.7%	8.3%	4.9%	5.3%	4.8%
Return on Equity	14.6%	16.4%	8.6%	16.3%	27.2%	20.1%	11.1%	11.7%	10.5%
ROIC	4.6%	6.1%	3.5%	7.3%	13.2%	10.7%	6.2%	6.8%	6.3%
Shares Out.	157.7	159.2	160.5	161.3	160.1	158.2	157.8	157.8	159.2
Revenue/Share	6.99	7.30	4.86	4.90	5.11	5.74	6.09	6.08	6.98
FCF/Share	0.45	0.68	0.37	0.70	(0.15)	0.48	0.04	0.46	0.59

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