



MDU Resources (MDU)

Updated February 19th, 2023, by Josh Arnold

Key Metrics

Current Price:	\$32	5 Year CAGR Estimate:	8.0%	Market Cap:	\$6.4 B
Fair Value Price:	\$32	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	03/08/23
% Fair Value:	102%	5 Year Valuation Multiple Estimate:	-0.3%	Dividend Payment Date:	04/01/23
Dividend Yield:	2.8%	5 Year Price Target	\$42	Years Of Dividend Growth:	32
Dividend Risk Score:	A	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

MDU Resources is a regulated energy delivery, transportation, and construction materials and services business. The company was founded back in 1924 and since that time, it has grown from a small electric utility in North Dakota to a market capitalization of \$6.4 billion. It has paid more than 80 consecutive years of dividends and operates electric and gas utilities, pipelines, and construction businesses. It should generate \$6.9 billion in sales this year, and about 75% of that will come from the company's construction businesses; utility businesses make up the remaining ~25%.

MDU reported fourth quarter and full-year earnings on February 9th, 2023, and results were better than expected on both the top and bottom lines, and by wide margins in both cases. Adjusted-earnings-per-share came to 61 cents, which was eight cents better than estimates. Revenue soared 29% year-over-year to \$1.86 billion, and was \$360 million ahead of expectations. On a dollar basis, adjusted earnings were \$126 million, which was sharply higher than the \$87 million in the year-ago period. On a per-share basis, it was up from 42 cents.

MDU had an all-time high backlog at the end of the year of \$3 billion in its construction businesses.

The electric and natural gas utility earned \$102 million in 2022, which was down fractionally year-over-year. The segment experienced higher volumes from colder weather, but higher operating and maintenance expenses saw earnings struggle to move higher.

The construction services business saw record earnings of \$125 million for the year, while the construction materials business earned \$116 million.

The company is moving forward with its plan to separate into two publicly-traded companies, as it is set to spin off its Knife River business in the second quarter of this year.

We start 2023 with an earnings-per-share estimate of \$2.10, which would represent a new record, and a return to growth, if achieved.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$1.53	\$1.40	\$0.90	\$1.15	\$1.46	\$1.39	\$1.69	\$1.95	\$1.87	\$1.87	\$2.10	\$2.81
DPS	\$0.52	\$0.72	\$0.74	\$0.76	\$0.77	\$0.80	\$0.82	\$0.83	\$0.85	\$0.88	\$0.89	\$1.01
Shares	189	194	195	196	196	196	199	201	204	203	202	200

Earnings-per-share have bounced around in recent years, owed to the very cyclical nature of its construction business that is somewhat – but not fully – offset by the steady utilities and pipeline businesses. MDU offers a bit of an odd mix in this way but when performance is robust, growth can be strong. Our earnings growth forecast is 6% annually because the construction business may suffer during a prolonged downturn, but that appears to be no threat at this point. Indeed, the construction business continues to set records, but has begun to show some cracks in recent results given constraints outside of the company's control. Inflationary pressures are causing lower earnings estimates, but we believe this will be transitory. We will also wait and see if the planned separation of Knife River consummates, and what impact that will have on growth estimates for MDU.

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The company can achieve this expansion via sales growth, both organically and through acquisitions. With a record backlog and very strong results from the construction business, we think MDU's future is bright. However, growth in 2020 and 2021 was sizable and we think building on that will prove somewhat challenging, with stagnant earnings in 2022 the result of this. On top of MDU's growing, diverse streams of revenue, margins are moving higher in the construction business, providing another tailwind to earnings growth when things are good. But keep in mind the risk of its cyclical nature, particularly in the construction business, and some of this has begun to show in recent results in terms of lower profit margins.

We forecast the dividend to continue its very modest rate of growth, moving up to \$1.01 from the current 89 cents.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	17.4	22.1	22.0	19.6	18.4	19.5	15.8	12.4	16.4	16.2	15.2	15.0
Avg. Yld.	2.0%	2.3%	3.7%	3.3%	2.9%	2.9%	3.1%	3.4%	2.8%	2.9%	2.8%	2.4%

MDU's price-to-earnings multiple has moved around a lot, which is something you would expect for a cyclical company. The multiple is now 15.2 times this year's earnings given the rise in expected earnings. Our fair value estimate of 15 times earnings means the stock is essentially fairly valued today.

The yield could decline slightly as we believe the earnings multiple will moderate some. MDU's capital allocation strategy calls for plenty of acquisitions as well as paying the dividend.

Safety, Quality, Competitive Advantage, & Recession Resiliency

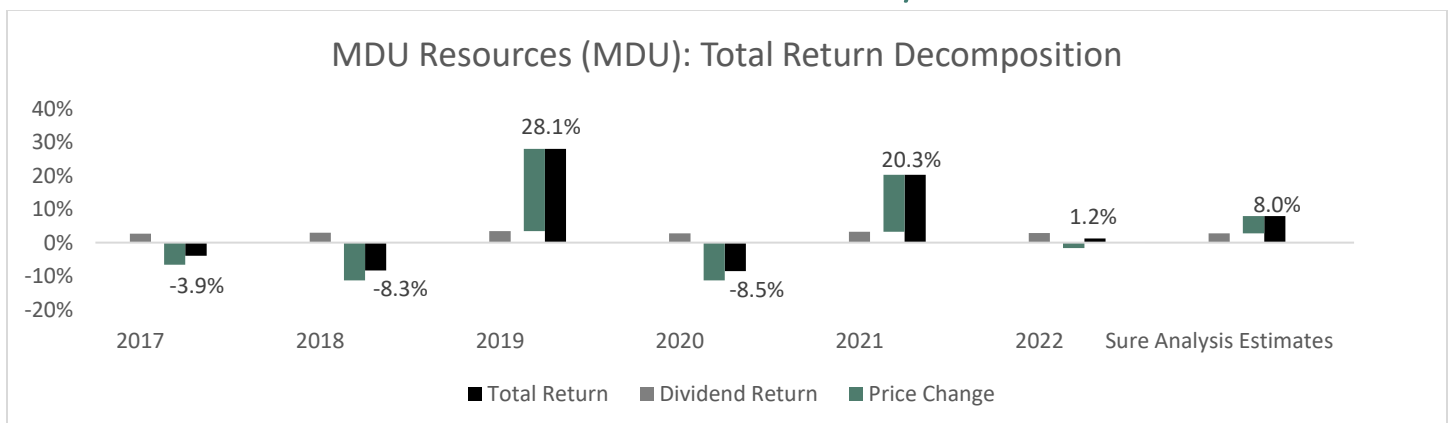
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	34%	52%	82%	65%	53%	58%	49%	43%	45%	47%	42%	36%

MDU's payout ratio is less than half of earnings, so it is considered safe. We expect small levels of dividend growth under that of earnings growth. MDU's competitive advantage can also be its downfall in that it operates a utility and pipeline business that are both stable, but it is also in construction, which is one of the most cyclical industries. This gives MDU a major leg up on other utilities in the good times but can be its downfall in times of economic hardship.

Final Thoughts & Recommendation

We forecast 8% annual total returns going forward for MDU consisting of the 2.8% current yield, a 0.3% headwind from the valuation, and 6% earnings-per-share growth. We are reiterating MDU at a hold rating, and note that total returns have improved since our last update.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	4075	3920	4115	4014	4129	4443	4532	5337	5533	5681
Gross Profit	946	662	675	672	777	798	791	933	1047	1045
Gross Margin	23.2%	16.9%	16.4%	16.8%	18.8%	18.0%	17.4%	17.5%	18.9%	18.4%
Operating Profit	411	321	327	320	409	424	402	481	545	534
Operating Margin	10.1%	8.2%	8.0%	8.0%	9.9%	9.5%	8.9%	9.0%	9.8%	9.4%
Net Profit	-1	279	298	-622	64	281	272	335	390	378
Net Margin	0.0%	7.1%	7.2%	-15.5%	1.6%	6.3%	6.0%	6.3%	7.1%	6.7%
Free Cash Flow	(288)	223	158	125	74	107	(68)	(34)	768	(164)
Income Tax	(31)	74	64	71	93	65	47	63	85	89

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	6682	7061	7832	6565	6284	6335	6988	7683	8053	8910
Cash & Equivalents	49	45	82	84	46	35	54	66	60	54
Inventories	317	282	289	241	238	227	287	278	291	336
Goodwill & Int. Ass.	653	649	645	643	638	636	676	697	740	788
Total Liabilities	4034	4205	4583	4045	3968	3906	4421	4836	4974	5528
Accounts Payable	388	405	279	286	280	312	359	403	426	479
Long-Term Debt	1773	1866	2094	1796	1790	1715	2109	2243	2263	2742
Shareholder's Equity	2633	2808	3119	2382	2301	2429	2567	2847	3079	3383
LTD/E Ratio	0.67	0.66	0.67	0.75	0.77	0.71	0.82	0.79	0.81	0.81

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.0%	4.1%	4.0%	-8.6%	1.0%	4.5%	4.1%	4.6%	5.0%	4.5%
Return on Equity	0.0%	10.3%	10.1%	-22.6%	2.8%	11.9%	10.9%	12.4%	13.2%	11.7%
ROIC	0.0%	6.1%	5.9%	-12.9%	1.5%	6.8%	6.2%	8.9%	7.5%	6.6%
Shares Out.	189	189	194	195	196	196	196	199	201	202
Revenue/Share	21.58	20.67	21.37	20.59	21.11	22.71	23.10	26.87	27.58	28.07
FCF/Share	(1.53)	1.18	0.82	0.64	0.38	0.54	(0.35)	(0.17)	3.83	(0.81)

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

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