



MDU Resources (MDU)

Updated May 7th, 2023, by Josh Arnold

Key Metrics

Current Price:	\$29	5 Year CAGR Estimate:	10.1%	Market Cap:	\$6 B
Fair Value Price:	\$32	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	06/10/23
% Fair Value:	92%	5 Year Valuation Multiple Estimate:	1.7%	Dividend Payment Date:	07/01/23
Dividend Yield:	3.1%	5 Year Price Target	\$42	Years Of Dividend Growth:	32
Dividend Risk Score:	A	Retirement Suitability Score:	B	Rating:	Buy

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 billion. It has paid more than 80 consecutive years of dividends and operates electric and gas utilities, pipelines, and construction businesses. It should generate \$7 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 posted first quarter earnings on May 4th, 2023, and results were better than expected on both revenue and profits. Adjusted earnings-per-share came to 23 cents, which was three cents ahead of estimates. Revenue soared 22.5% year-over-year to \$1.74 billion, and was \$360 million ahead of expectations.

MDU noted its intended separation of its construction materials business, Knife River Corporation, is approved for a May 31st distribution to shareholders of record as of May 22nd. Knife River will be publicly traded after the separation and will be listed on the NYSE.

The company issued guidance for this year of regulated energy delivery earnings of \$140 million to \$150 million. In addition, construction services revenue is expected to be \$2.8 billion to \$3.0 billion, with higher margins, and EBITDA of \$200 million to \$225 million. Construction materials revenue is expected to be \$2.5 billion to \$2.7 billion, with higher margins and EBITDA of \$300 million to \$350 million.

We've left our estimate of \$2.10 in earnings-per-share for this year unchanged from initial guidance.

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 seem to have abated. 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.

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

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its cyclicality, 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	13.8	15.0
Avg. Yld.	2.0%	2.3%	3.7%	3.3%	2.9%	2.9%	3.1%	3.4%	2.8%	2.9%	3.1%	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 13.8 times this year's earnings given the rise in expected earnings. Our fair value estimate of 15 times earnings means the stock is now somewhat undervalued.

The yield could decline 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

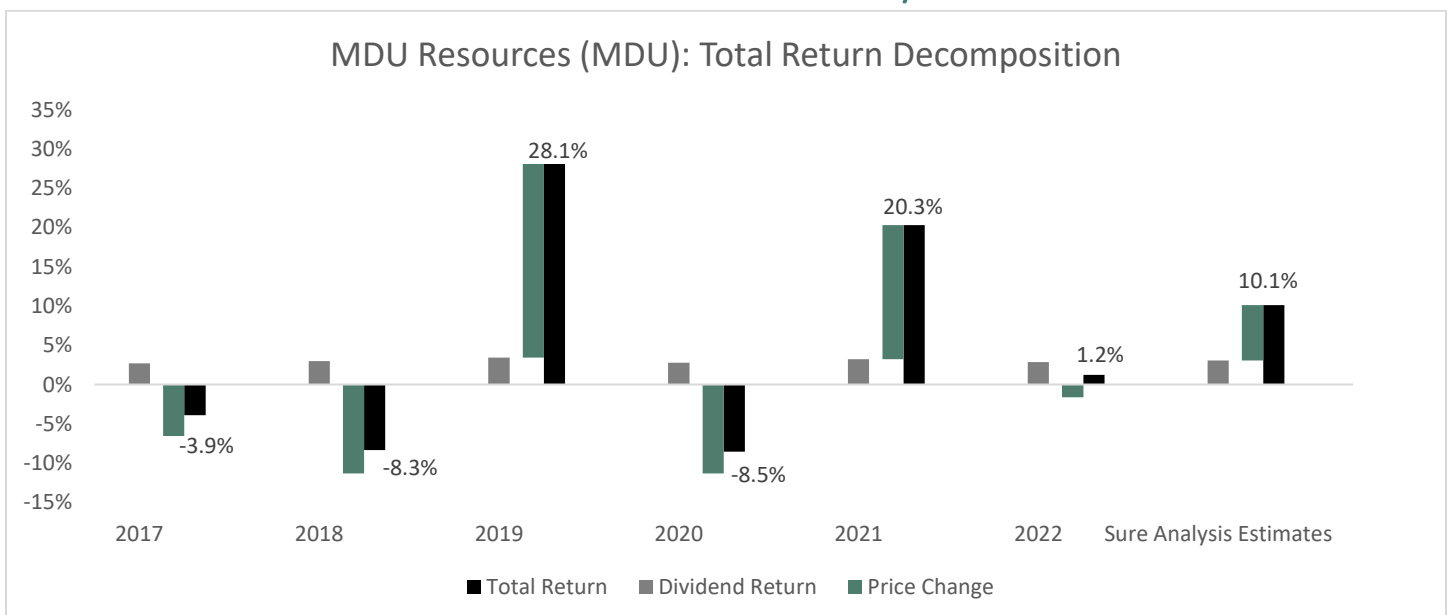
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	34%	52%	82%	65%	53%	58%	49%	43%	45%	47%	42%	36%

MDU's payout ratio is less than half of earnings, so it is considered safe. We expect small levels of dividend growth below 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 10.1% annual total returns going forward for MDU consisting of the 3.1% current yield, a 1.7% tailwind from the valuation, and 6% earnings-per-share growth. We are upgrading MDU to a buy 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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	3920	4115	4014	4129	4443	4532	5337	5533	5681	6974
Gross Profit	662	675	672	777	798	791	933	1047	1045	1145
Gross Margin	16.9%	16.4%	16.8%	18.8%	18.0%	17.4%	17.5%	18.9%	18.4%	16.4%
Operating Profit	321	327	320	409	424	402	481	545	534	574
Operating Margin	8.2%	8.0%	8.0%	9.9%	9.5%	8.9%	9.0%	9.8%	9.4%	8.2%
Net Profit	279	298	-622	64	281	272	335	390	378	367
Net Margin	7.1%	7.2%	-15.5%	1.6%	6.3%	6.0%	6.3%	7.1%	6.7%	5.3%
Free Cash Flow	223	158	125	74	107	(68)	(34)	768	(164)	(147)
Income Tax	74	64	71	93	65	47	63	85	89	95

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	7061	7832	6565	6284	6335	6988	7683	8053	8910	9661
Cash & Equivalents	45	82	84	46	35	54	66	60	54	81
Inventories	282	289	241	238	227	287	278	291	336	388
Goodwill & Int. Ass.	649	645	643	638	636	676	697	740	788	781
Total Liabilities	4205	4583	4045	3968	3906	4421	4836	4974	5528	6074
Accounts Payable	405	279	286	280	312	359	403	426	479	657
Long-Term Debt	1866	2094	1796	1790	1715	2109	2243	2263	2742	3088
Shareholder's Equity	2808	3119	2382	2301	2429	2567	2847	3079	3383	3587
LTD/E Ratio	0.66	0.67	0.75	0.77	0.71	0.82	0.79	0.81	0.81	0.86

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	4.1%	4.0%	-8.6%	1.0%	4.5%	4.1%	4.6%	5.0%	4.5%	4.0%
Return on Equity	10.3%	10.1%	-22.6%	2.8%	11.9%	10.9%	12.4%	13.2%	11.7%	10.5%
ROIC	6.1%	5.9%	-12.9%	1.5%	6.8%	6.2%	8.9%	7.5%	6.6%	5.7%
Shares Out.	189	194	195	196	196	196	199	201	202	203
Revenue/Share	20.67	21.37	20.59	21.11	22.71	23.10	26.87	27.58	28.07	34.23
FCF/Share	1.18	0.82	0.64	0.38	0.54	(0.35)	(0.17)	3.83	(0.81)	(0.72)

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

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