



Middlesex Water (MSEX)

Updated July 31st, 2023 by Samuel Smith

Key Metrics

Current Price:	\$80.6	5 Year CAGR Estimate:	3.8%	Market Cap:	\$1.4 B
Fair Value Price:	\$78.6	5 Year Growth Estimate:	2.7%	Ex-Dividend Date:	8/10/23
% Fair Value:	103%	5 Year Valuation Multiple Estimate:	-0.5%	Dividend Payment Date:	9/1/23
Dividend Yield:	1.6%	5 Year Price Target	\$90	Years Of Dividend Growth:	50
Dividend Risk Score:	A	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

Middlesex Water Company was formed in 1897. The company is a water and wastewater utility in New Jersey and Delaware. Its market capitalization is \$1.4 billion. Middlesex has paid consecutive dividends since 1912 and has reached its 50th consecutive year of dividend increases.

On July 28th, 2023, Middlesex reported second quarter results. In Q2 2023, revenues increased by \$3.1 million to \$42.8 million compared to the same period in 2022. The rise was primarily driven by higher revenues from the Middlesex and Pinelands systems, as well as increased non-regulated revenues. Operations and maintenance expenses increased by \$1.6 million due to higher production costs and labor expenses. Income taxes decreased by \$1.1 million, leading to a net income increase of \$1.0 million, resulting in diluted earnings per share of \$0.55 for Q2 2023.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$1.03	\$1.13	\$1.22	\$1.38	\$1.38	\$1.96	\$2.02	\$2.18	\$2.07	\$2.12	\$2.62	\$3.00
DPS	\$0.75	\$0.76	\$0.78	\$0.81	\$0.86	\$0.96	\$0.98	\$1.05	\$1.11	\$1.18	\$1.25	\$1.50
Shares¹	16.0	16.1	16.2	16.3	16.4	16.4	17.4	17.5	17.5	17.6	17.7	20.0

Earnings-per-share have been rising steadily over the past decade, although gains have been far from linear. The Great Recession saw earnings fall markedly in 2009 but recovery was fairly quick and since 2009, earnings have roughly tripled. We see annualized earnings-per-share growth for the next five years in the low-single-digits as the meaningful sources of growth will be the rate increase in New Jersey, and inflationary pressures. Adding customers will also help some as it will also improve operational efficiencies through economies of scale.

We are forecasting the dividend to continue its streak of small increases, rising to \$1.50 in five years' time. Middlesex has an impressive streak of dividend increases that will continue to grow but on a percentage basis, the payout will rise rather slowly. The company's payout ratio was far too high during the Great Recession and management pulled way back on dividend increases to avoid a similar fate down the road.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	19.7	18.5	19.1	25.6	28.4	26.9	30.5	34.2	56.4	36.5	30.8	30.0
Avg. Yld.	3.7%	3.6%	3.3%	2.3%	2.2%	1.8%	1.6%	1.4%	1.0%	1.5%	1.6%	1.7%

The company's price-to-earnings multiple looks slightly overvalued today. As a result, the stock should face a modest headwind to total returns in the coming half decade from multiple compression. The dividend yield will likely remain in its current range moving forward as dividend growth will likely modestly outpace earnings while being offset by multiple expansion.

¹ In millions

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Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	73%	67%	64%	59%	62%	49%	49%	48%	54%	56%	48%	50%

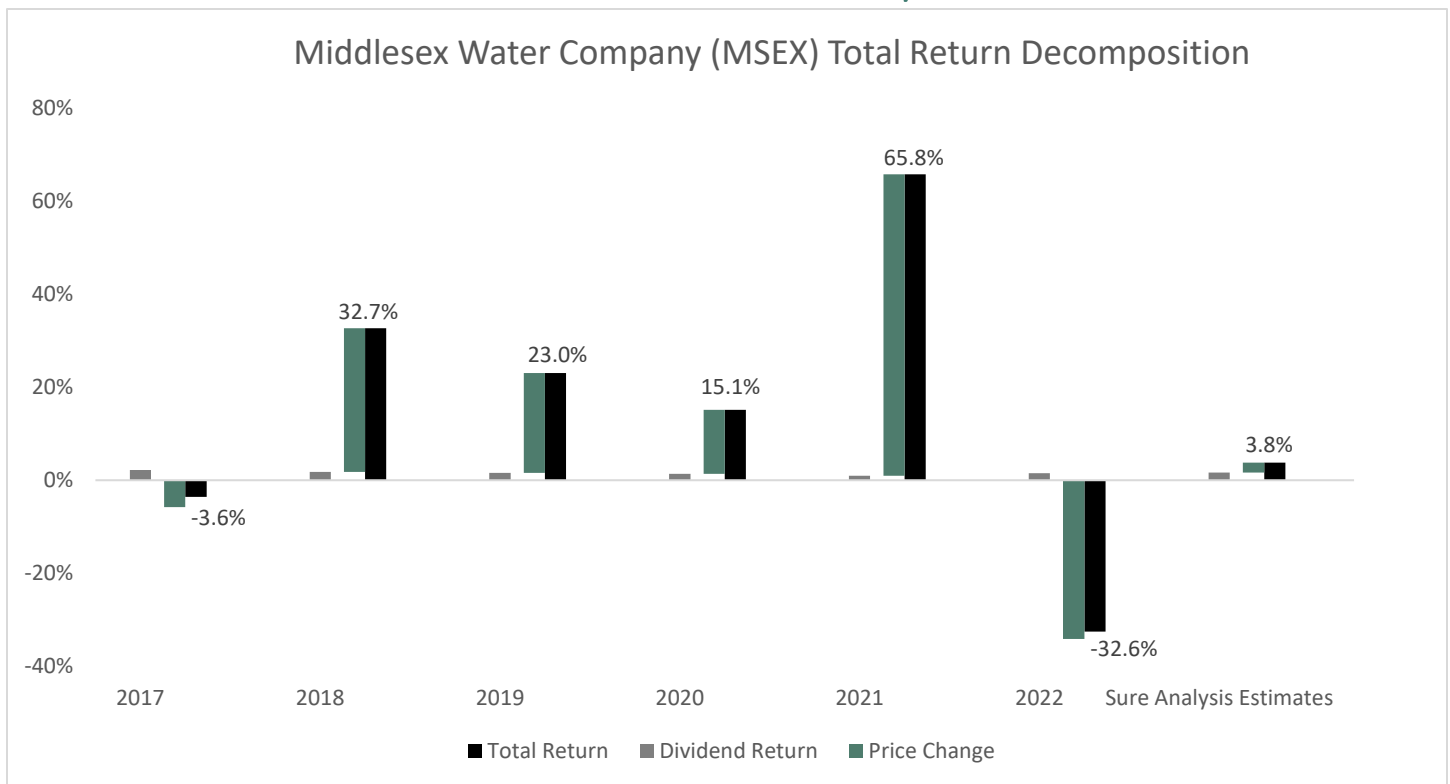
Like many other regulated utilities, Middlesex' quality metrics have remained steady in the past decade thanks to the monopoly-like nature of its assets. However, since pricing is regulated, they cannot drive excessive profitability, thereby explaining the resistance to significant margin expansion. Its assets are mostly debt-financed, allowing for an excellent interest coverage ratio for a utility. Middlesex has the balance sheet to weather virtually any economic storm so there is no question of safety, but obviously growth remains an issue. The payout ratio neared 100% in 2009 but slow growth in dividends and better rates of earnings-per-share growth have led it back down to 48% today, making the dividend very safe.

Middlesex' recession performance is decent given that it sells the most basic staple of all and indeed, its revenue was basically flat in 2009 at the height of the recession. Its earnings did not fare quite as well, but it certainly stood up to the downturn. Its obvious competitive advantage is in the monopoly it enjoys in its service area.

Final Thoughts & Recommendation

Middlesex offers annualized total return potential of 3.8% going forward based on our projections, as the current yield and low single digit expected annual earnings-per-share growth will be partially offset by expected valuation multiple compression. The company's impressive dividend growth history is certainly worth noting but the current yield is likely too low to attract income investors. Middlesex would also be unattractive for those seeking growth or value, given the low potential for the former and high current valuation. As a result, we rate the stock a Hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	115	117	126	133	131	138	135	142	143	162
D&A Exp.	12	12	13	14	15	16	17	21	27	83
Operating Profit	31	34	36	40	38	37	36	37	33	51.3%
Operating Margin	27.0%	29.4%	28.4%	30.3%	28.9%	26.9%	26.4%	26.4%	23.2%	27
Net Profit	17	18	20	23	23	32	34	38	37	44
Net Margin	14.5%	15.7%	15.9%	17.1%	17.4%	23.5%	25.2%	27.1%	25.5%	27.3%
Free Cash Flow	14	10	25	(0)	(7)	(26)	(53)	(52)	(46)	42
Income Tax	9	10	11	12	11	1	(3)	(4)	(5)	26.1%

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	530	576	581	620	661	768	910	976	1,020	1,074
Cash & Equivalents	5	3	3	4	5	4	2	4	4	4
Accounts Receivable	12	10	10	10	11	12	12	15	15	16
Inventories	2	2	3	4	4	5	5	5	5	6
Total Liabilities	339	376	372	399	430	517	584	628	650	672
Accounts Payable	6	6	7	12	14	19	23	30	21	25
Long-Term Debt	164	161	142	153	174	209	258	282	326	363
Shareholder's Equity	189	197	207	218	229	249	324	346	368	400
LTD/E Ratio	0.85	0.81	0.68	0.69	0.75	0.83	0.79	0.81	0.88	0.90

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	3.0%	3.3%	3.5%	3.8%	3.6%	4.5%	4.0%	4.1%	3.7%	4.1%
Return on Equity	9.0%	9.6%	9.9%	10.7%	10.2%	13.6%	11.8%	11.5%	10.2%	11.0%
ROIC	4.7%	5.2%	5.6%	6.3%	5.9%	7.5%	6.5%	6.3%	5.5%	5.8%
Shares Out.	16.0	16.1	16.2	16.3	16.4	16.4	17.4	17.5	17.5	17.6
Revenue/Share	7.13	7.22	7.72	8.09	7.93	8.35	8.00	8.06	8.13	9.17
FCF/Share	0.85	0.61	1.56	(0.02)	(0.45)	(1.59)	(3.15)	(2.97)	(2.63)	(1.69)

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

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