



MGE Energy (MGEE)

Updated November 13th, 2023 by Samuel Smith

Key Metrics

Current Price:	\$71.1	5 Year CAGR Estimate:	4.5%	Market Cap:	\$2.6B
Fair Value Price:	\$59.7	5 Year Growth Estimate:	5.7%	Ex-Dividend Date:	11/30/23
Fair Value:	119%	5 Year Valuation Multiple Estimate:	-3.4%	Dividend Payment Date:	12/15/23
Dividend Yield:	2.4%	5 Year Price Target	\$79	Years of Dividend Growth:	46
Dividend Risk Score:	A	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

MGE Energy has grown from a small power station in Wisconsin built in 1902 to a \$2.6 billion market capitalization integrated energy company. The company has paid consecutive dividends for more than 100 years and has raised its payout for the past 46 years. MGE principally operates gas and electric utilities, in addition to transmission and construction businesses.

On November 2, 2023, MGE Energy Inc. (NASDAQ: MGEE) reported its financial results for the third quarter of 2023. The company recorded GAAP (Generally Accepted Accounting Principles) earnings of \$37.9 million, which translates to \$1.05 per share. This marked a significant increase from the \$33.7 million, or \$0.93 per share, reported for the same period in the previous year. A key factor contributing to this increase was the earnings from investment in ATC, which rose by \$0.9 million. Moreover, the company observed a 5% increase in electric residential sales, which also played a crucial role in boosting its earnings. Despite these gains, the gas net income for Q3 2023 remained relatively flat when compared to Q3 2022.

This strong performance demonstrates MGE Energy's ability to grow its earnings and maintain a stable financial position, even in a challenging economic environment. The growth in earnings per share and the increase in electric residential sales suggest that the company is effectively managing its resources and investments to generate positive returns. The flat performance in gas net income, while not contributing to growth, indicates a level of stability in that segment of the business. Overall, these results reflect positively on MGE Energy's financial health and strategic direction.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$2.16	\$2.32	\$2.06	\$2.18	\$2.20	\$2.43	\$2.50	\$2.60	\$2.92	\$3.07	\$3.41	\$4.50
DPS	\$1.07	\$1.11	\$1.16	\$1.21	\$1.26	\$1.35	\$1.39	\$1.44	\$1.52	\$1.63	\$1.71	\$2.20
Shares¹	34.7	34.7	34.7	34.7	34.7	34.7	34.7	36.2	36.2	36.2	36.2	37

Earnings-per-share have grown consistently over the past decade, though they did encounter a brief bump in the road in 2015. Recent results have been strong, and we believe that between its two sustainable growth catalysts of customer acquisition and renewable asset growth, the company should be able to achieve mid-single-digit earnings-per-share growth going forward. Investors would do well to consider that weather can contribute positively but can easily swing results in the other direction. We see mid-single-digit growth for the dividend as well as MGE is comfortable with where the payout ratio is today. MGE is on par with other utilities in terms of dividend growth in the mid-single-digits.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	17	17.2	20.3	24.9	22.9	26.7	31.6	27.4	24.9	22.5	20.9	17.5
Avg. Yld.	2.9%	2.8%	2.8%	2.2%	2.5%	2.1%	1.8%	2.0%	2.1%	2.4%	2.4%	2.8%

¹ In millions

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MGE's price-to-earnings multiple has moved significantly higher in the past half decade to the mid-20s to low 30s. It sits at 20.9 times earnings today, and as a result, we believe MGE is still overvalued. The lack of robust earnings growth it has exhibited and a lack of catalysts for it to pick up in the coming years mean that the current multiple seems unsustainable. Thus, we are forecasting a headwind to annual total returns in the coming years from multiple contraction.

The dividend yield is also telling us the stock is overvalued as it is still in the lower end of its range over the past decade. We think the combination of continued payout growth and a stock price that should come down over time will produce a higher, more normalized 2.8% yield against the current 2.4%. The current valuation multiple for MGE has not only made the stock expensive, but it has made the dividend less attractive as well.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	50%	48%	56%	56%	57%	56%	56%	55%	52%	53%	50%	49%

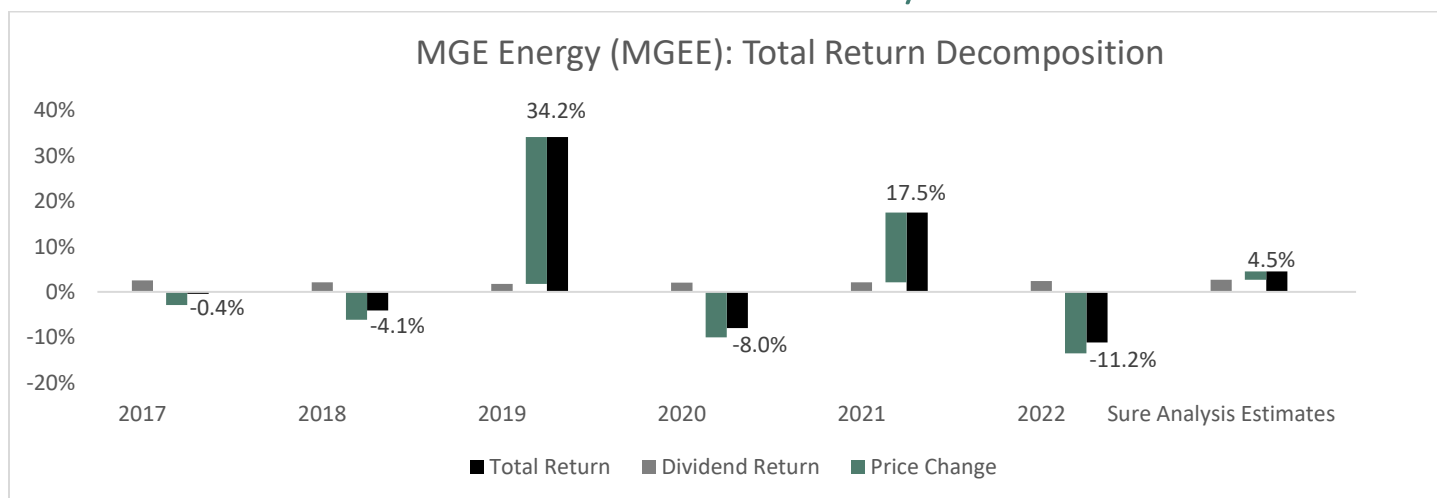
MGE's quality metrics have been roughly flat over the past decade, as it does not go after growth via acquisition, and its business has not really changed. Gross margins have drifted up over time but appear to have plateaued. MGE's interest coverage is outstanding for a utility, and we forecast this will improve slightly over time as earnings grow and MGE keeps its debt at manageable levels. The payout ratio should remain around 50% as dividend growth will likely lag earnings growth, but the two should be very close. Overall, MGE is conservatively financed and run basically the same way year after year, meaning changes in the quality metrics will likely be few and far between.

MGE's main competitive advantage is its virtual monopoly in its service area. Like many other utilities, MGE has a small but profitable service area where it is continuing to grow its customer base. That helped it hold up well in the Great Recession as earnings-per-share dipped slightly but then recovered quickly.

Final Thoughts & Recommendation

Overall, MGE appears slightly overvalued right now. We are forecasting total annualized returns for the next five years to be 4.5% as multiple contraction will offset some of the dividend and earnings-per-share growth. MGE has failed to grow its earnings faster than a mid-single-digit rate, but the valuation is pricing in a bit more growth than that. MGE therefore is rated a Hold right now.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	591	620	564	545	563	560	569	539	607	715
Gross Profit	185	198	188	189	198	190	202	204	214	244
Gross Margin	31.4%	32.0%	33.4%	34.6%	35.2%	33.9%	35.6%	37.9%	35.2%	34.1%
Operating Profit	39	41	44	45	53	56	72	74	77	86
Operating Margin	128	138	124	124	126	114	111	110	117	138
Net Profit	21.7%	22.3%	22.0%	22.7%	22.3%	20.4%	19.5%	20.4%	19.3%	19.3%
Net Margin	75	80	71	76	50	84	87	92	106	111
Free Cash Flow	12.7%	13.0%	12.6%	13.9%	8.8%	15.0%	15.3%	17.2%	17.4%	15.5%
Income Tax	21	36	69	64	23	(59)	(34)	(31)	(16)	(21)

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,579	1,694	1,726	1,801	1,855	1,989	2,082	2,254	2,372	2,518
Cash & Equivalents	69	66	81	96	108	83	23	45	17	12
Accounts Receivable	45	42	37	40	42	44	40	41	46	55
Inventories	36	46	48	41	44	42	45	47	52	74
Total Liabilities	962	1,035	1,036	1,077	1,077	1,172	1,226	1,278	1,344	1,436
Accounts Payable	44	42	41	48	48	46	55	55	64	59
Long-Term Debt	404	406	391	387	427	511	543	577	625	710
Shareholder's Equity	618	659	690	724	778	817	856	976	1,027	1,082
LTD/E Ratio	0.65	0.62	0.57	0.53	0.55	0.63	0.64	0.59	0.61	0.66

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	4.7%	4.9%	4.2%	4.3%	2.7%	4.4%	4.3%	4.3%	4.6%	4.5%
Return on Equity	12.5%	12.6%	10.6%	10.7%	6.6%	10.6%	10.4%	10.1%	10.6%	10.5%
ROIC	7.6%	7.7%	6.6%	6.9%	4.3%	6.7%	6.4%	6.3%	6.6%	6.4%
Shares Out.	34.7	34.7	34.7	34.7	34.7	34.7	34.7	36.2	36.2	36.2
Revenue/Share	17.04	17.88	16.27	15.71	16.24	16.15	16.41	15.13	16.77	19.75
FCF/Share	0.61	1.04	1.99	1.85	0.67	(1.71)	(0.97)	(0.86)	(0.43)	(0.59)

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