



Middlesex Water (MSEX)

Updated March 11th, 2024 by Samuel Smith

Key Metrics

Current Price:	\$51.5	5 Year CAGR Estimate:	8.8%	Market Cap:	\$0.9 B
Fair Value Price:	\$56.5	5 Year Growth Estimate:	4.7%	Ex-Dividend Date:	5/15/24 ¹
% Fair Value:	91%	5 Year Valuation Multiple Estimate:	1.9%	Dividend Payment Date:	6/1/24 ²
Dividend Yield:	2.5%	5 Year Price Target	\$71	Years Of Dividend Growth:	51
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 \$0.9 billion. Middlesex has paid consecutive dividends since 1912 and has reached its 51st consecutive year of dividend increases.

On February 29, 2024, Middlesex Water Company (MSEX) reported their financial results for the fourth quarter of 2023. In the fiscal year ending December 31, 2023, consolidated operating revenues rose to \$166.3 million, marking a \$3.8 million increase from 2022. This growth was driven by various factors including a net \$4.2 million increase in Middlesex System revenues due to the final phase implementation of a 2021 base rate case increase and additional revenues from the Purchase Water Adjustment Clause rate. However, Tidewater System revenues experienced a net decrease of \$0.9 million due to lower customer connection fees, decreased weather-driven customer demand, and a rate reduction ordered by the Delaware Public Service Commission in September 2022. The Pinelands System in New Jersey saw a \$0.2 million increase due to a base rate increase effective April 15, 2023, while non-regulated operations revenues increased by \$0.3 million due to higher supplemental contract services. Operating and maintenance expenses for the year increased to \$83.1 million, primarily attributed to higher variable production costs, elevated chemical prices, and increased labor costs. Depreciation expenses also rose by \$2.2 million due to a higher level of utility plant in service. Middlesex realized a \$5.2 million gain from selling its regulated Delaware wastewater subsidiary in January 2022. Income taxes decreased by \$2.2 million, largely due to greater tax benefits associated with increased repair expenditures on tangible property in the Middlesex system. Consequently, net income for the year declined to \$31.5 million, compared to \$42.4 million in 2022, with earnings applicable to common stock totaling \$31.4 million, or \$1.76 per share on a fully diluted basis, down from \$42.3 million or \$2.39 per diluted share in 2022.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	\$1.13	\$1.22	\$1.38	\$1.38	\$1.96	\$2.02	\$2.18	\$2.07	\$2.12	\$1.76	\$2.26	\$2.85
DPS	\$0.76	\$0.78	\$0.81	\$0.86	\$0.96	\$0.98	\$1.05	\$1.11	\$1.18	\$1.26	\$1.30	\$1.50
Shares³	16.1	16.2	16.3	16.4	16.4	17.4	17.5	17.5	17.6	17.8	17.8	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 mid-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

¹ Estimated

² Estimated

³ In millions

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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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	19.7	18.5	19.1	25.6	28.4	26.9	30.5	34.2	56.4	36.5	22.8	25.0
Avg. Yld.	3.4%	3.5%	3.1%	2.4%	1.7%	1.8%	1.6%	1.6%	1.0%	2.0%	2.5%	2.1%

The company's price-to-earnings multiple looks slightly undervalued today. As a result, the stock should enjoy a slight tailwind to total returns in the coming half-decade from multiple expansion. The dividend yield will likely remain in its current range moving forward as dividend growth will likely modestly outpace earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	67%	64%	59%	62%	49%	49%	48%	54%	56%	72%	58%	53%

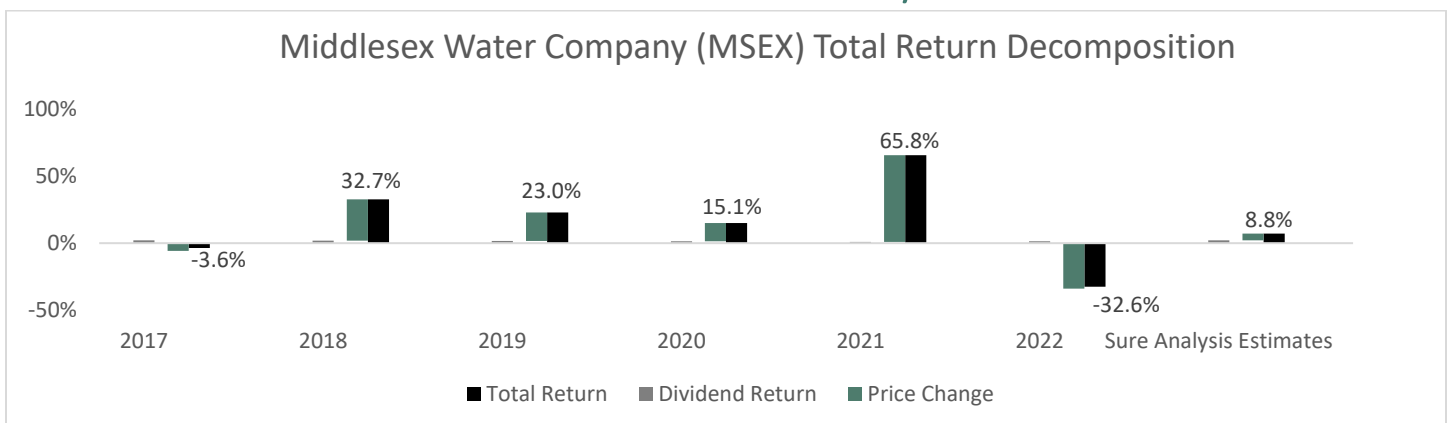
Like many other regulated utilities, Middlesex' quality metrics have remained steady in the past decade thanks to the monopoly-like nature of its assets. However, since pricing is regulated, they cannot drive excessive profitability, thereby explaining the resistance to significant margin expansion. 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 58% 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 8.8% going forward based on our projections, as the current yield and mid-single digit expected annual earnings-per-share growth will combine with slight expected valuation multiple expansion. 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	117	126	133	131	138	135	142	143	162	166
D&A Exp.	12	13	14	15	16	17	21	27	27	29
Operating Profit	34	36	40	38	37	36	37	33	42	39
Operating Margin	29.4%	28.4%	30.3%	28.9%	26.9%	26.4%	26.4%	23.2%	25.9%	23.6%
Net Profit	18	20	23	23	32	34	38	37	42	32
Net Margin	15.7%	15.9%	17.1%	17.4%	23.5%	25.2%	27.1%	25.5%	26.1%	19.0%
Free Cash Flow	10	25	(0)	(7)	(26)	(53)	(52)	(46)	(30)	(37)
Income Tax	10	11	12	11	1	(3)	(4)	(5)	3	1

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	576	581	620	661	768	910	976	1,020	1,074	1,236
Cash & Equivalents	3	3	4	5	4	2	4	4	4	2
Accounts Receivable	10	10	10	11	12	12	15	15	16	18
Inventories	2	3	4	4	5	5	5	5	6	7
Total Liabilities	376	372	399	430	517	584	628	650	672	811
Accounts Payable	6	7	12	14	19	23	30	21	25	28
Long-Term Debt	161	142	153	174	209	258	282	326	363	409
Shareholder's Equity	197	207	218	229	249	324	346	368	400	423
LTD/E Ratio	0.81	0.68	0.69	0.75	0.83	0.79	0.81	0.88	0.90	0.96

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	3.3%	3.5%	3.8%	3.6%	4.5%	4.0%	4.1%	3.7%	4.1%	2.7%
Return on Equity	9.4%	9.8%	10.6%	10.1%	13.4%	11.7%	11.4%	10.2%	11.0%	7.6%
ROIC	5.2%	5.6%	6.3%	5.9%	7.5%	6.5%	6.3%	5.5%	5.8%	3.9%
Shares Out.	16.1	16.2	16.3	16.4	16.4	17.4	17.5	17.5	17.6	17.8
Revenue/Share	7.22	7.72	8.09	7.93	8.35	8.00	8.06	8.13	9.17	9.32
FCF/Share	0.61	1.56	(0.02)	(0.45)	(1.59)	(3.15)	(2.97)	(2.63)	(1.69)	(2.10)

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

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