

**COMPANY UPDATE /  
ESTIMATE CHANGE**
**Key Metrics**

ARTNA - NASDAQ - as of 1/17/18	\$38.25
Price Target	--
52-Week Range	\$29.83 - \$43.22
Shares Outstanding (mm)	9.3
Market Cap. (\$mm)	\$355.2
1-Mo. Average Daily Volume	24,211
Institutional Ownership	45.7%
LT Debt/Total Capital	Q3'17 42.3%
ROE	TTM 9.3%
Book Value / Share	Q3'17 \$15.57
Price / Book Value	2.5x
Dividend Yield	2.5%
EBITDA Margin	FY'16 45.9%

**EPS FY 12/31**

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	\$0.31	--	\$0.34	A --	\$0.35
2Q	\$0.33	--	\$0.35	A --	\$0.37
3Q	\$0.48		\$0.42	A --	\$0.47
4Q	\$0.30	\$0.31	\$0.31	--	\$0.37
Year	\$1.41	\$1.42	\$1.43	\$1.50	\$1.56
P/E	27.1x		26.7x		24.5x

**Revenue (\$mm)**

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	\$18.4	--	\$19.3	A --	\$19.7
2Q	\$19.4	--	\$20.5	A --	\$21.2
3Q	\$21.8		\$22.4	A --	\$23.3
4Q	\$19.4	\$20.2	\$20.2	--	\$21.4
Year	\$79.1	\$82.3	\$82.3	\$85.5	\$85.6

**Company Description:** *Artesian Resources Corp., through its wholly owned subsidiary, Artesian Water Company, provides water service to approximately 85,000 metered customers, and has a customer base of ~275,000 residents in DE, MD, and PA. It sells water to residential, commercial, industrial, governmental, municipal, and utility customers, and also provides wastewater treatment services.*

**Water Utilities**

Analyst: Spencer E. Joyce, CFA  
502.588.8402 // sjoyce@hilliard.com  
Institutional Sales Desk: George Moorin  
502.588.9141 // gmoorin@hilliard.com  
J.J.B. Hilliard, W.L. Lyons, LLC  
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**Artesian Resources Corp.**

ARTNA — NASDAQ — Neutral-3

**Initiating 2019 Estimates, Reiterating Neutral Rating.**
**Investment Highlights**

- We are initiating a 2019 EPS estimate of \$1.60 on revenue of just under \$90MM.
- At this time, our 2017E EPS rises a penny to \$1.43 due to rounding and a mix of minute model tweaks; our 2018E EPS rises a more consequential \$0.06, primarily as we adjust our model to reflect a reduction in interest expense tied to a rate lock for notes coming due January 2018.
- Substantially underpinning our growth projections over 2018/2019 is our expectation for a base rate case filing in Delaware this spring. Artesian does not guide toward rate activity, although our view here is supported by ARTNA's normal filing cadence over the past several cycles.
- Furthermore, with Utility operating expenses up 7% and Cap ex up 40% YTD (through Q3), and with ROE likely to decline in 2017 versus 2016 (by our model), we believe the company is reasonably well-positioned from a financial standpoint to file a case.
- Qualitatively, growth in 2019 looks fairly similar to what we expect in 2018. Interim rates and a subsequent final award mean a general rate filing could have incremental impact in both years, and we expect fairly steady customer growth (1%) to persist.
- We are reiterating our Neutral rating. Valuation from a long-term risk/reward standpoint is fine, in our view, although with a reduced tactical affinity for water utilities in early 2018, we remain patient.
- ARTNA recently declared a dividend payable 2/23/18; back in November, the Board approved a dividend increase of 1.5%, or ~3% on an annualized basis.
- With no interim guidance from Artesian, we refrain from adjusting our model for tax concerns at this time. Having said that, we expect our core EPS targets to be little changed by recent US tax cuts; we do ultimately expect some (offsetting) model revisions.
- We expect ARTNA to report Q4'17 results in March.

**Note Important Disclosures on Pages 5-6  
Note Analyst Certifications on Page 5**

**SUITABILITY**

We assign ARTNA a suitability rating of '3.' A complete description of our suitability scale is on page 5. Artesian's small-cap status, relatively low trading volume and a lack of regional diversification versus most Utility sector peers keep ARTNA below our '2' suitability rating. Industry-appropriate leverage, tenured monopoly franchises and a seemingly amicable regulatory environment keep ARTNA well above our most aggressive '4' rating.

**CONSIDERATIONS AND RISKS**

We view all companies in the Water Utilities industry as being subject to significant regulatory and political risk. Utility operations are heavily regulated; negative rate-making climates and/or new environmental restrictions may affect the company's ability to earn a sufficient return on invested capital. Weather, natural disaster, and availability of water supplies could negatively impact sources of water, demand for water services, and a utility's ability to supply water to customers. Risks associated with the collection, treatment, and disposal of wastewater could also impose significant costs.

Significant capital expenditures are required to maintain infrastructure and expand rate base. Should the company suffer from a lack of ability to secure appropriate funding to make investments, or if delays are incurred in completing projects, operating results could be negatively affected. Contamination of water could result in service interruptions or cause enforcement actions. Water assets can be subject to condemnation through eminent domain.

Artesian operates with limited geographical diversity. As such, the company's operating results may be more sensitive to negative events that directly affect its regions of operations. Additionally, the company is subject to all other risks that result from operating as a publicly traded company.

Our Suitability rating is 3 on a 1-to-4 scale (1 = most conservative, 4 = most aggressive).

*Additional information is available upon request.*



## Artesian Resources Corp.

Summary Balance Sheet	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17	Q3'17	Q4'17E	FY'17E	FY'18E	FY'19E
Cash	\$243	\$209	\$511	\$223	\$244	\$226	\$226	\$200	\$303	\$250	\$110	\$110	\$1,740	\$1,080
A/R	5,065	6,350	5,809	7,885	7,849	7,796	7,796	6,000	6,796	7,245	8,130	8,130	8,580	8,850
Other CAs	11,340	7,885	5,770	5,879	7,786	6,613	6,613	5,981	5,808	8,898	6,750	6,750	6,890	7,030
Total Current Assets	16,648	14,444	12,090	13,987	15,879	14,635	14,635	12,181	12,907	16,393	14,990	14,990	17,210	16,960
Net PP&E	393,793	405,606	407,173	413,642	419,952	425,502	425,502	430,749	438,259	447,762	452,750	452,750	480,190	508,900
Other	11,772	11,576	11,543	11,329	11,108	10,839	10,839	15,555	15,467	15,308	11,060	11,060	11,280	11,510
<b>Total Assets</b>	<b>422,213</b>	<b>431,626</b>	<b>\$430,806</b>	<b>\$438,958</b>	<b>\$446,939</b>	<b>\$450,976</b>	<b>450,976</b>	<b>\$458,485</b>	<b>\$466,633</b>	<b>\$479,463</b>	<b>\$478,800</b>	<b>478,800</b>	<b>508,680</b>	<b>537,370</b>
LOC	18,491	10,487	6,466	4,818	4,008	7,130	7,130	3,892	1,183	6,300	11,800	11,800	23,700	4,000
A/P	3,783	4,914	3,052	3,633	4,402	5,532	5,532	4,341	3,404	5,761	5,770	5,770	6,090	6,280
Accrued Exp	1,513	1,254	1,501	2,205	2,570	1,309	1,309	2,506	3,200	3,531	1,090	1,090	860	630
Other CLs	6,405	6,563	6,419	6,796	9,913	5,357	5,357	32,227	36,423	7,640	5,460	5,460	5,570	5,680
Total Current Liabilities	30,192	23,218	17,438	17,452	20,893	19,328	19,328	42,966	44,210	23,232	24,120	24,120	36,220	16,590
LTD	104,954	103,647	103,259	102,992	102,599	102,331	102,331	81,533	81,262	105,860	105,580	105,580	104,790	133,660
Def Income Tax	57,043	62,156	63,518	64,711	66,449	68,453	68,453	69,695	70,607	74,678	69,140	69,140	69,830	70,530
Net CIAC	92,429	99,847	102,842	108,118	110,868	112,106	112,106	114,352	118,679	121,544	122,290	122,290	125,290	128,290
Other	11,990	10,427	10,212	10,297	10,253	9,735	9,735	9,466	9,336	9,565	9,930	9,930	10,130	10,330
Shareholders' Equity	125,605	132,331	133,537	135,388	135,877	139,023	139,023	140,473	142,539	144,584	147,740	147,740	162,420	177,970
<b>Total Liab &amp; SE</b>	<b>\$422,213</b>	<b>\$431,626</b>	<b>\$430,806</b>	<b>\$438,958</b>	<b>\$446,939</b>	<b>\$450,976</b>	<b>450,976</b>	<b>\$458,485</b>	<b>\$466,633</b>	<b>\$479,463</b>	<b>\$478,800</b>	<b>478,800</b>	<b>508,680</b>	<b>537,370</b>
Summary Cash Flow	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17	Q3'17	Q4'17E	FY'17E	FY'18E	FY'19E
Net Income	\$9,506	\$11,305	\$2,830	\$3,041	\$4,360	\$2,723	\$12,954	\$3,086	\$3,251	\$3,942	\$2,920	\$13,200	\$14,640	\$15,100
D&A	8,673	8,837	2,315	2,249	2,270	2,353	9,188	2,319	2,329	2,377	2,510	9,540	10,140	10,750
Deferred Tax	7,255	5,097	543	1,188	1,733	1,633	5,097	1,237	908	4,066	750	6,960	3,000	3,000
(Inc) / Dec in Wrk Cap	(7,103)	3,200	897	(523)	2,380	(3,461)	(707)	2,304	3,330	(2,634)	(3,350)	(350)	(390)	(340)
Operating Cash Flow	18,331	28,439	6,585	5,955	10,743	3,248	26,532	8,946	9,818	7,751	2,830	29,350	27,390	28,510
Cap Ex	(23,730)	(20,694)	(4,270)	(7,780)	(7,954)	(8,247)	(28,251)	(7,664)	(9,436)	(11,184)	(7,500)	(35,780)	(37,580)	(39,460)
Dividends	(7,523)	(7,811)	(2,010)	(2,042)	(2,047)	(2,081)	(8,180)	(2,084)	(2,121)	(2,128)	(2,190)	(8,520)	(8,960)	(9,290)
Free Cash Flow	(12,922)	(66)	305	(3,867)	742	(7,080)	(9,899)	(802)	(1,739)	(5,561)	(6,860)	(14,950)	(19,150)	(20,240)
Net Adv and CIAC	3,808	5,829	3,214	4,495	2,156	42	9,907	2,128	3,880	2,396	1,000	9,400	8,000	8,400
LTD Proceeds	689	-	-	-	-	-	-	-	-	-	-	-	25,000	30,000
LTD (Repay)	(1,132)	(1,263)	(379)	(263)	(383)	(264)	(1,289)	(290)	(267)	(392)	(280)	(1,230)	(26,120)	(1,120)
Net LOC Borrow / (Repay)	8,159	(8,004)	(4,021)	(1,648)	(4,106)	6,418	(3,357)	(3,238)	1,303	3,711	5,500	7,280	11,900	(19,700)
Stock Issued	1,651	3,049	386	830	225	385	1,826	414	643	183	500	1,740	2,000	2,000
Net Cash Flow	253	(455)	(495)	(453)	(1,366)	(499)	(2,812)	(1,788)	3,820	337	(140)	2,240	1,630	(660)
EBITDA	\$ 31,094	\$ 34,203	\$ 8,120	\$ 8,941	\$ 10,713	\$ 8,564	\$ 36,338	\$ 8,405	\$ 9,082	\$ 10,377	\$ 9,010	\$ 36,880	\$ 39,030	\$ 41,530
EV / TTM EBITDA	9.9x	10.4x	10.3x	12.1x	10.4x	10.9x	10.9x	10.4x	12.2x	12.5x	12.6x	12.6x	11.9x	11.9x
Selected Financial Statistics	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17	Q3'17	Q4'17E	FY'17E	FY'18E	FY'19E
Book Value	\$ 14.04	\$ 14.55	\$ 14.63	\$ 14.79	\$ 14.81	\$ 15.13	\$ 15.13	\$ 15.26	\$ 15.43	\$ 15.57	\$ 15.86	\$ 15.86	\$ 17.23	\$ 18.85
Price / Book	1.6x	1.9x	1.9x	2.3x	1.9x	2.1x	2.1x	2.1x	2.6x	2.4x	2.4x	2.4x	2.2x	2.0x
LTD / Total Cap	45.5%	43.9%	43.6%	43.2%	43.0%	42.4%	42.4%	36.7%	36.3%	42.3%	41.7%	41.7%	39.2%	42.9%
ROE (TTM)	7.7%	8.8%	9.0%	8.7%	9.1%	9.6%	9.6%	9.7%	9.7%	9.3%	9.2%	9.2%	9.4%	8.8%

Source: Company reports and Hilliard Lyons estimates

### **Analyst Certification**

I, Spencer E. Joyce, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

### **Important Disclosures**

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

### **Suitability Ratings**

- 1** - A large cap, core holding with a solid history
- 2** - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks
- 3** - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage
- 4** - Speculative, due to small size, inconsistent profitability, erratic revenues, volatility, low trading volume or a narrow customer or product base

### **Investment Ratings**

**Buy** - We believe the stock has significant total return potential in the coming 12 months.

**Long-term Buy** - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

**Neutral** - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

**Underperform** - We believe the stock is vulnerable to a price setback in the next 12 months.



Rating	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	31	28%	10%	90%
Hold/Neutral	75	67%	9%	91%
Sell	6	5%	0%	100%

As of 8 January 2018

**Other Disclosures**

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