

**COMPANY UPDATE /
ESTIMATE CHANGE**
Key Metrics

ARTNA - NASDAQ - as of 11/2/17	\$41.39
Price Target	--
52-Week Range	\$27.13 - \$43.22
Shares Outstanding (mm)	9.3
Market Cap. (\$mm)	\$384.3
1-Mo. Average Daily Volume	21,209
Institutional Ownership	45.3%
LT Debt/Total Capital	Q3'17 42.3%
ROE	TTM 9.3%
Book Value / Share	Q3'17 \$15.57
Price / Book Value	2.7x
Dividend Yield	2.3%
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 --	--
2Q	\$0.33	--	\$0.35	A --	--
3Q	\$0.48		\$0.42	A --	--
4Q	\$0.30	\$0.32	\$0.31	--	--
Year	\$1.41	\$1.46	\$1.42	\$1.55	\$1.50
P/E	29.4x		29.1x		27.6x

Revenue (\$mm)

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	\$18.4	--	\$19.3	A --	--
2Q	\$19.4	--	\$20.5	A --	--
3Q	\$21.8	--	\$22.4	A --	--
4Q	\$19.4	\$20.2	\$20.2	--	--
Year	\$79.1	\$82.0	\$82.3	\$85.2	\$85.5

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

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Artesian Resources Corp.

ARTNA — NASDAQ — Neutral-3

Q3'17 Results, Reiterating Neutral Rating.
Investment Highlights

- Artesian reported Q3'17 EPS of \$0.42 vs. \$0.48 in Q3'16; EPS fell \$0.03 short of our target, which was the sole published estimate. A modest decline in operating income due to core revenue/expense items largely fell to the bottom line; a higher effective tax rate (39.2% vs 36.4%) was a headwind as well.
- Nonetheless, core operational performance was fine, in our view, as we continue to view 2017 as a baseline year ahead of potential rate activity in 2018.
- Total revenue grew 2.4% to \$20.05MM in the third quarter, outpacing our estimate by 110 basis point. DSIC surcharges were an incremental driver, partially offset by lower usage (usually a function of weather).
- Utility operating expenses grew 8.4% in Q3, well ahead of our estimate for +2.5% and driving much of the EPS miss versus our target. Total Op Ex (inclusive of D&A and non-utility) was higher by 7.5% yr/yr.
- This second sequential quarter of upper single digit expense growth feeds into our view that a rate case in DE is likely to be filed in Spring 2018. We note that the company does not 'guide' for rate case activity.
- YTD Cap Ex through September 30 was \$28.3MM, up materially from \$20.0MM in the prior-year period. In line with our typical utility framework, this bodes well for growth moving forward, in our view.
- Reflecting downside to Q3 and higher expenses assumptions in Q4, our 2017E EPS slides \$0.04 to \$1.42. In sympathy, our 2018E EPS falls a nickel to \$1.50, but continues to mark a return to growth. Our 2018 model year remains sensitive to developments in our rate outlook.
- We are reiterating our Neutral rating. We like the story with re-accelerating capital spend and a potential rate case next year; however, we believe investors could see a more compelling entry point

**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	Q3'17p	Q4'17E	FY'17E	FY'18E
Cash	\$243	\$209	\$511	\$223	\$244	\$226	\$226	\$200	\$303	\$900	\$2,970	\$2,970	\$3,680
A/R	5,065	6,350	5,809	7,885	7,849	7,796	7,796	6,000	6,796	8,040	8,110	8,110	8,570
Other CAs	11,340	7,885	5,770	5,879	7,786	6,613	6,613	5,981	5,808	7,453	6,750	6,750	6,890
Total Current Assets	16,648	14,444	12,090	13,987	15,879	14,635	14,635	12,181	12,907	16,393	17,830	17,830	19,140
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	480,210
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
Total Assets	422,213	431,626	\$430,806	\$438,958	\$446,939	\$450,976	450,976	\$458,485	\$466,633	\$479,463	\$481,640	481,640	510,630
LOC	18,491	10,487	6,466	4,818	4,008	7,130	7,130	3,892	1,183	9,180	14,680	14,680	30,280
A/P	3,783	4,914	3,052	3,633	4,402	5,532	5,532	4,341	3,404	4,510	5,760	5,760	6,080
Accrued Exp	1,513	1,254	1,501	2,205	2,570	1,309	1,309	2,506	3,200	2,370	1,090	1,090	860
Other CLs	6,405	6,563	6,419	6,796	9,913	5,357	5,357	32,227	36,423	7,172	5,460	5,460	5,570
Total Current Liabilities	30,192	23,218	17,438	17,452	20,893	19,328	19,328	42,966	44,210	23,232	26,990	26,990	42,790
LTD	104,954	103,647	103,259	102,992	102,599	102,331	102,331	81,533	81,262	105,860	82,700	82,700	105,570
Def Income Tax	57,043	62,156	63,518	64,711	66,449	68,453	68,453	69,695	70,607	67,110	69,140	69,140	69,830
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
Other	11,990	10,427	10,212	10,297	10,253	9,735	9,735	9,466	9,336	17,133	9,930	9,930	10,130
Shareholders' Equity	125,605	132,331	133,537	135,388	135,877	139,023	139,023	140,473	142,539	144,584	170,590	170,590	157,020
Total Liab & SE	\$422,213	\$431,626	\$430,806	\$438,958	\$446,939	\$450,976	450,976	\$458,485	\$466,633	\$479,463	\$481,640	481,640	510,630
Summary Cash Flow	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17	Q3'17p	Q4'17E	FY'17E	FY'18E
Net Income	\$9,506	\$11,305	\$2,830	\$3,041	\$4,360	\$2,723	\$12,954	\$3,086	\$3,251	\$3,942	\$2,890	\$13,170	\$14,040
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
Deferred Tax	7,255	5,097	543	1,188	1,733	1,633	5,097	1,237	908	750	750	3,650	3,000
(Inc) / Dec in Wrk Cap	(7,103)	3,200	897	(523)	2,380	(3,461)	(707)	2,304	3,330	(4,864)	(1,110)	(340)	(390)
Operating Cash Flow	18,331	28,439	6,585	5,955	10,743	3,248	26,532	8,946	9,818	2,205	5,040	26,020	26,790
Cap Ex	(23,730)	(20,694)	(4,270)	(7,780)	(7,954)	(8,247)	(28,251)	(7,664)	(9,436)	(11,200)	(7,500)	(35,800)	(37,600)
Dividends	(7,523)	(7,811)	(2,010)	(2,042)	(2,047)	(2,081)	(8,180)	(2,084)	(2,121)	(2,150)	(2,190)	(8,550)	(8,960)
Free Cash Flow	(12,922)	(66)	305	(3,867)	742	(7,080)	(9,899)	(802)	(1,739)	(11,145)	(4,650)	(18,330)	(19,770)
Net Adv and CIAC	3,808	5,829	3,214	4,495	2,156	42	9,907	2,128	3,880	1,000	1,000	8,010	4,000
LTD Proceeds	689	-	-	-	-	-	-	-	-	-	-	-	25,000
LTD (Repay)	(1,132)	(1,263)	(379)	(263)	(383)	(264)	(1,289)	(290)	(267)	(280)	(280)	(1,120)	(26,120)
Net LOC Borrow / (Repay)	8,159	(8,004)	(4,021)	(1,648)	(4,106)	6,418	(3,357)	(3,238)	1,303	8,000	5,500	11,570	15,600
Stock Issued	1,651	3,049	386	830	225	385	1,826	414	643	500	500	2,060	2,000
Net Cash Flow	253	(455)	(495)	(453)	(1,366)	(499)	(2,812)	(1,788)	3,820	(1,925)	2,070	2,190	710
EBITDA	\$ 31,094	\$ 34,203	\$ 8,120	\$ 8,941	\$ 10,713	\$ 8,564	\$ 36,338	\$ 8,405	\$ 9,082	\$ 10,377	\$ 8,980	\$ 36,850	\$ 38,930
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	12.6x
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
Book Value	\$ 14.04	\$ 14.55	\$ 14.63	\$ 14.79	\$ 14.81	\$ 15.13	\$ 15.13	\$ 15.26	\$ 15.43	\$ 15.57	\$ 18.32	\$ 18.32	\$ 16.66
Price / Book	1.6x	1.9x	1.9x	2.3x	1.9x	2.1x	2.1x	2.1x	2.6x	2.4x	2.3x	2.3x	2.5x
LTD / Total Cap	45.5%	43.9%	43.6%	43.2%	43.0%	42.4%	42.4%	36.7%	36.3%	42.3%	32.7%	32.7%	40.2%
ROE (TTM)	7.7%	8.8%	9.0%	8.7%	9.1%	9.6%	9.6%	9.7%	9.7%	9.3%	8.9%	8.9%	8.9%

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.



Hilliard Lyons Recommended Issues			Investment Banking Provided in Past 12 Mo.	
Rating	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	39	32%	8%	92%
Hold/Neutral	74	60%	9%	91%
Sell	8	7%	0%	100%
Restriction	2	2%	100%	0%

As of 5 October 2017

Other Disclosures

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