



## COMPANY UPDATE / TARGET CHANGE ESTIMATE CHANGE

### Key Metrics

CPK - NYSE - as of	7/31/17	\$77.25
Price Target		\$97.00
52-Week Range	\$57.63 -	\$77.75
Shares Outstanding (mm)		16.3
Market Cap. (\$mm)		\$1,261.9
1-Mo. Average Daily Volume		52,251
Institutional Ownership		63.0%
LT Debt/Total Capital	Q1'17	22.9%
ROE	TTM	10.4%
Book Value / Share	Q1'17	\$28.19
Price / Book Value		2.7x
Dividend Yield		1.7%
LTM EBITDA Margin		21.2%

### EPS FY 12/31

	2016A	Prior 2017E	Current 2017E	Prior 2018E	Current 2018E
1Q	\$1.33	--	\$1.17	A --	--
2Q	\$0.52	\$0.47	\$0.46	--	--
3Q	\$0.29	\$0.38	\$0.38	--	--
4Q	\$0.73	\$0.91	\$0.91	--	--
Year	\$2.86	\$2.92	\$2.91	\$3.57	\$3.48
P/E	27.0x		26.5x		22.2x

\*adjusted for special items

### Total Firm Gross Margin (\$MM)

	2016A	Prior 2017E	Current 2017E	Prior 2018E	Current 2018E
1Q	\$77.4	--	\$84.2	A --	--
2Q	\$57.8	\$60.1	\$60.1	--	--
3Q	\$55.5	\$62.0	\$62.0	--	--
4Q	\$70.2	\$79.1	\$79.1	--	--
Year	\$260.8	\$285.4	\$285.4	\$320.1	\$317.1

**Company Description:** Chesapeake Utilities Corp. is a diversified utility company engaged in natural gas distribution, transmission and marketing, electric distribution, propane gas distribution and wholesale marketing, advanced information services, and other related services. Its service territories include portions of Delaware, Maryland, and Florida.

### Natural Gas Utilities

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August 1, 2017

## Chesapeake Utilities Corp.

CPK — NYSE — Long-term Buy-3

**Cautious ahead of Q2'17 Results for CPK, but Raising Price Target to \$97 and Initiating 2019 Estimates.**

### Investment Highlights

- CPK is scheduled to report Q2 results on the morning of Thursday 8/4, with a conference call on Friday 8/5.
- Tactically we are cautious ahead of the report, given shares making an all-time high intra-day today and our expectation for Q2'17 EPS of \$0.47, which is \$0.05 below both consensus and year-ago EPS.
- By CPK standards, we model just modest margin growth for Q2, but believe reflation of cost structure (O&M—healthcare, business development) could holdover as a theme from Q1.
- Nonetheless, we retain our Long-term Buy rating given an unchanged view that CPK represents a best-in-class growth story in the gas utility industry. In line with our longer-term investment thesis we extend our price target in tandem with rolling out 2019 estimates.
- We are initiating 2019E EPS of \$3.86 on gross margin of \$337.7MM; in our view, current consensus at \$3.62 is too low. We expect regulated expansion(s) to drive most of the growth.
- At this time, our 2017/2018 EPS estimates fall to \$2.91/\$3.48 (-\$0.01/-0.09), as we tweak our margin growth table and slide our expense assumptions slightly higher.
- We are raising our 2-year price target to \$97 from \$81 previously. At our target, CPK would trade ~25x our 2019E EPS, which is in line with where the industry currently trades based on 2017 consensus estimates.
- Our valuation allowances extend slightly at this time, based in part on market conditions and partially on our view that CPK is increasingly worthy of an industry-multiple due to its relative growth rate, increased size/scope/market cap, and a more regulated (or regulated-like) business mix.

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

**ADDITIONAL DISCUSSION—FORWARD OUTLOOK & FINAL THOUGHTS**

As noted in our opening points, we view the consensus 2019 profit forecast as too low. We concede that our model assumes some incremental impact from expansions and/or initiatives that are not-yet-announced; however, given recent history at CPK, gas industry dynamics, and our qualitative interpretation of the project/M&A pipeline, we actually view this as more conservative than a forecast that might assert no new projects. Our 2019 model assumes negligible gross margin growth from the non-regulated segment (over 2018); this view will assuredly evolve as we work through the next couple of years, and likely presents both upside and downside risk.

A (potentially) weaker quarter (Q2'17) is not likely to alter our investment thesis in CPK, although we regularly look for period-to-period dislocations in stock prices across the market as potential entry points. As such, we elect to reiterate our multi-year bullish stance toward CPK and retain our positive rating at this point, with the caveat that we do not necessarily see the need be overly aggressive before Q2 earnings hit the wire in just a couple of trading sessions.

**SUITABILITY**

We assign CPK a suitability rating of '3.' A complete description of our suitability scale is on page 5. Smaller than most diversified utility peers, we see a path for Chesapeake to outpace average growth across the utility sector over an extended timeframe; this growth outlook is accompanied by a slightly elevated risk profile due to reliance on individual discrete projects. CPK's material exposure to non-regulated operations brings an element of cyclical to earnings, which helps push the stock below our more conservative '2' rating. Alternatively, below-sector leverage, generally consistent earnings/cash flow/dividends, multiple regulated franchises with monopoly status, and secular tailwinds for growth keep CPK well above our speculative/most aggressive '4' rating.

**CONSIDERATIONS AND RISKS**

Utility operations are weather sensitive. Warmer weather can lead to lower total margin from lower volumes of natural gas sold or transported, while extremely cold weather may lead to conservation by customers in order to reduce consumption.

Gas utilities face competition from alternative fuels. In the industrial market, many customers have the capability of using both natural gas as well as another source of energy. Increases in the price of natural gas can negatively impact a competitive position by decreasing the price benefits of natural gas to the end user.

Gas utilities are subject to regulation at the federal and state levels. Regulatory commissions and policies vary from state to state, and have a significant bearing on profitability.

CPK has been acquisitive in recent years, and we expect CPK may remain a net buyer of assets over the next few years. Risk from a growth-by-acquisition strategy includes: potential for additional growth to not materialize, overpayment for assets (impairments), managerial distraction and stressing the balance sheet.

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

*Additional information is available upon request.*

Chesapeake Utilities Corp.														
Income Statements (000's)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E	FY'19E
Regulated Revenue	\$300,442	\$301,902	\$89,216	\$67,395	\$70,019	\$79,059	\$305,689	\$97,654						
Regulated Cost of Sales	134,560	122,814	34,905	21,635	24,644	28,425	109,609	40,244						
Regulated Energy Gross Margin	165,882	179,088	54,311	45,760	45,375	50,634	196,080	57,410	47,700	49,150	55,560	209,820	239,200	259,600
Unregulated Revenue	184,961	162,108	57,080	34,947	38,329	67,417	203,778	87,506	38,160	42,300	67,390	235,360	243,490	242,990
Other Revenue	13,431	(4,766)	-	-	-	(4,602)	(10,607)	-	-	-	-	-	0	0
Unreg & Other energy cost of sales	143,556	97,228	34,024	22,934	28,183	43,291	128,434	60,754	25,760	29,430	43,820	159,760	164,920	164,920
UnReg & Other Gross Margin	54,836	60,114	23,056	12,013	10,146	19,524	64,737	26,752	12,400	12,870	23,570	75,600	78,570	78,070
Total Firm Gross Margin	220,718	239,202	77,367	57,773	55,521	70,158	260,817	84,162	60,100	62,020	79,130	285,420	317,770	337,670
Operating Expenses														
Operations	102,197	107,562	27,159	28,087	30,126	32,200	117,571	32,913	29,490	31,630	33,970	128,003	134,740	140,120
Maintenance	9,706	11,803	2,479	2,904	3,542	3,466	12,391	3,231	3,050	3,720	3,640	13,641	14,320	14,900
Impairment	6,881	-	-	-	-	-	-	-	-	-	-	-	-	-
D & A	26,316	29,972	7,503	7,780	8,209	8,667	32,159	8,812	8,990	9,660	10,370	37,832	43,410	46,480
Other Tax	13,339	13,607	3,846	3,390	3,488	4,006	14,730	4,530	3,420	3,520	4,050	15,520	15,680	15,840
Total Operating Expenses	158,439	161,444	40,987	42,031	45,365	48,339	176,721	49,486	44,950	48,530	52,030	194,996	208,150	217,340
Operating Income	62,279	77,758	36,380	15,742	10,156	21,819	84,096	34,676	15,150	13,490	27,100	90,424	109,620	120,330
Gain on Sale	7,139	0					-							
Other Income, Net	101	293	(34)	(8)	(28)	(372)	(441)	(277)	50	50	50	(130)	200	200
Interest	9,482	10,006	2,650	2,624	2,722	2,643	10,639	2,739	3,020	3,170	3,640	12,570	16,620	17,130
EBT	60,037	68,045	33,696	13,110	7,406	18,804	73,016	31,660	12,180	10,370	23,510	77,724	93,200	103,400
Income Tax	23,945	26,905	13,329	5,081	2,990	6,941	28,341	12,516	4,730	4,190	8,680	30,116	36,360	40,370
Net Income--Cont'd Ops	36,092	41,140	20,367	8,029	4,416	11,863	44,675	19,144	7,450	6,180	14,830	47,608	56,840	63,030
Net Income	\$36,092	\$41,140	\$20,367	\$8,029	\$4,416	\$11,863	\$44,675	\$19,144	\$7,450	\$6,180	\$14,830	\$47,608	\$56,840	\$63,030
Diluted Avg Shares	14,605	15,143	15,331	15,353	15,413	16,349	15,613	16,349	16,349	16,349	16,349	16,349	16,349	16,349
EPS														
Continuing Ops	\$2.47	\$2.78	\$1.33	\$0.52	\$0.29	\$0.73	\$2.86	\$1.17	\$0.46	\$0.38	\$0.91	\$2.91	\$3.48	\$3.86
Ex.Special Items	\$2.47	\$2.72												
Dividends	\$1.0667	\$1.1325	\$0.2875	\$0.3050	\$0.3050	\$0.3050	\$1.2025	\$0.3050	\$0.3250	\$0.3250	\$0.3250	\$1.2800	\$1.3750	\$1.4000
<b>Rate of Change Analysis:</b>														
Gross Margin	10.7%	8.4%	-1.1%	12.6%	9.3%	18.1%	9.0%	8.8%	4.0%	11.7%	12.8%	9.4%	11.3%	6.3%
Operating Income	-0.7%	24.9%	-4.3%	19.5%	-6.9%	34.9%	8.2%	-4.7%	-3.8%	32.8%	24.2%	7.5%	21.2%	9.8%
EPS	10.2%	10.4%	-9.9%	48.2%	-14.3%	29.0%	5.1%	-11.9%	-12.9%	31.9%	25.0%	1.7%	19.4%	10.9%
O+M Expense	13.1%	6.7%	0.0%	7.2%	16.1%	12.1%	8.9%	22.0%	5.0%	5.0%	5.5%	9.0%	5.2%	4.0%
EBITDA	10.1%	12.8%	-2.4%	13.6%	-1.0%	27.1%	7.9%	-0.9%	2.6%	26.1%	22.9%	10.3%	19.3%	9.0%
<b>Margin Analysis:</b>														
Operations/GM	46.3%	45.0%	35.1%	48.6%	54.3%	45.9%	45.1%	39.1%	49.1%	51.0%	42.9%	44.8%	42.4%	41.5%
Maintenance/GM	4.4%	4.9%	3.2%	5.0%	6.4%	4.9%	4.8%	3.8%	5.1%	6.0%	4.6%	4.8%	4.5%	4.4%
Other Tax/GM	6.0%	5.7%	5.0%	5.9%	6.3%	5.7%	5.6%	5.4%	5.7%	5.7%	5.1%	5.4%	4.9%	4.7%
Operating income/GM	28.2%	32.5%	47.0%	27.2%	18.3%	31.1%	32.2%	41.2%	25.2%	21.8%	34.2%	31.7%	34.5%	35.6%
Net Income/GM	16.4%	17.2%	26.3%	13.9%	8.0%	16.9%	17.1%	22.7%	12.4%	10.0%	18.7%	16.7%	17.9%	18.7%
Tax rate	39.9%	39.5%	39.6%	38.8%	40.4%	36.9%	38.8%	39.5%	38.8%	40.4%	36.9%	38.7%	39.0%	39.0%
								*1/1/17 new base rates DE distribution					*Expect ESNG major expansion online Q1	
								*1/27/17 base rate filing for ESNG					*Pensacola online Q2	
								*12/2016: new Sandpiper rates; Revenue Neutral yr-1						

Source: Company reports and Hilliard Lyons estimates

Chesapeake Utilities Corp.														
Summary Balance Sheet	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E	FY'19E
Cash	\$4,574	\$2,855	\$3,315	\$3,266	\$1,536	\$4,178	\$4,178	\$5,700	\$44,130	\$23,290	\$25,950	\$25,950	\$17,960	\$18,670
A/R	53,300	41,007	44,434	41,851	47,103	62,803	62,803	58,375	42,270	47,570	63,430	63,430	64,060	64,700
Propane Inventory	7,250	6,619	5,412	4,285	4,106	6,457	6,457	5,437	4,500	4,310	6,780	6,780	7,120	7,480
Other Current Assets	57,249	62,057	47,214	37,494	49,411	67,713	67,713	49,301	37,870	49,910	68,390	68,390	69,070	69,760
Total Current Assets	122,373	112,538	100,375	86,896	102,156	141,151	141,151	118,813	128,770	125,080	164,550	164,550	158,210	160,610
Net PP&E	689,762	854,950	881,229	908,807	936,048	986,664	986,664	1,018,317	1,069,330	1,119,670	1,169,300	1,169,300	1,245,890	1,354,410
Regulatory Assets	78,136	8,268	7,634	7,042	76,343	7,694	7,694	7,527	7,110	7,110	7,770	7,770	7,850	7,930
Goodwill	4,952	14,548	15,070	15,070	15,070	15,070	15,070	15,070	15,070	15,070	15,070	15,070	15,070	15,070
Other	9,246	78,282	77,676	79,232	10,893	78,640	78,640	78,584	80,020	11,000	79,430	79,430	80,220	81,020
Total Assets	\$904,469	\$1,068,586	\$1,081,984	\$1,097,047	\$1,140,510	\$1,229,219	\$1,229,219	\$1,238,311	\$1,300,300	\$1,347,930	\$1,436,120	\$1,436,120	\$1,507,240	\$1,619,040
CP/LT Debt	9,109	9,151	9,163	12,075	12,087	12,099	12,099	12,111	4,000	4,000	4,000	4,000	4,000	2,000
ST Borrowing	88,231	173,397	172,742	180,042	154,490	209,871	209,871	199,333	274,330	239,330	289,330	289,330	191,330	226,330
A/P	44,610	39,300	36,299	35,496	41,297	56,935	56,935	49,500	35,850	41,710	57,500	57,500	58,080	58,660
Other Current Liabilities	52,285	57,745	56,245	56,279	55,179	55,146	55,146	59,789	56,840	55,730	55,700	55,700	56,260	56,820
Total Current Liabilities	194,235	279,593	274,449	283,892	263,053	334,051	334,051	320,733	371,020	340,770	406,530	406,530	309,670	343,810
LTD	158,486	149,340	148,602	143,865	143,525	136,954	136,954	136,537	143,090	213,030	209,470	209,470	304,230	300,990
Deferred Income Tax	160,232	193,431	197,416	199,623	205,562	222,894	222,894	231,004	233,000	235,000	237,000	237,000	245,000	253,000
Accrued Asset Removal Cost	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Other LT Liabilities	91,194	88,084	87,265	90,113	90,070	89,234	89,234	89,208	91,010	90,970	90,130	90,130	91,030	91,940
Shareholders' Equity	300,322	358,138	374,252	379,554	438,300	446,086	446,086	460,829	462,180	468,160	492,990	492,990	557,310	629,300
Total Liab & SE	\$904,469	\$1,068,586	\$1,081,984	\$1,097,047	\$1,140,510	\$1,229,219	\$1,229,219	\$1,238,311	\$1,300,300	\$1,347,930	\$1,436,120	\$1,436,120	\$1,507,240	\$1,619,040
Book Value	\$20.51	\$23.38	\$24.41	\$24.72	\$28.44	\$27.29	\$27.29	\$28.19	\$28.27	\$28.64	\$30.15	\$30.15	\$34.09	\$38.49
Tangible BV	\$20.17	\$22.43	\$23.43	\$23.74	\$27.46	\$26.36	\$26.36	\$27.27	\$27.35	\$27.71	\$29.23	\$29.23	\$33.17	\$37.57
Price / Book	2.4x	2.4x	2.6x	2.7x	2.1x	2.5x	2.5x	2.5x	2.7x	2.7x	2.6x	2.6x	2.3x	2.0x
Equity / Total Cap (inc ST Debt + CP)	54.4%	52.1%	53.4%	53.3%	58.7%	55.7%	55.7%	57.4%	55.1%	51.9%	50.8%	50.8%	53.6%	55.2%
Net Indebtedness / Total Capital	45.6%	47.9%	46.6%	46.7%	41.3%	44.3%	44.3%	42.6%	44.9%	48.1%	49.2%	49.2%	46.4%	44.8%
LT Debt / Total Capital	34.5%	29.4%	28.4%	27.5%	24.7%	23.5%	23.5%	22.9%	23.6%	31.3%	29.8%	29.8%	35.3%	32.4%
<b>Summary Cash Flow</b>														
Net Income	\$36,092	\$41,140	\$20,367	\$8,029	\$4,416	\$11,863	\$44,675	\$19,144	\$7,450	\$6,180	\$14,830	\$47,600	\$56,840	\$63,030
D&A	32,893	36,950	9,149	9,570	10,131	10,643	39,493	10,751	8,990	9,660	10,370	39,770	43,410	46,480
Deferred Income Tax	22,235	20,520	4,326	1,836	5,842	19,253	31,257	7,849	1,930	6,130	20,220	36,130	37,940	39,830
(Inc.) dec. in working cap.	(2,774)	8,266	8,122	12,661	(12,289)	(20,748)	(12,254)	21,068	11,870	(12,400)	(21,050)	(510)	(510)	(550)
Operating C.F.	88,446	106,876	41,964	32,096	8,100	21,011	103,171	58,812	30,240	9,570	24,370	122,990	137,680	148,790
Cap Ex	(97,164)	(144,618)	(36,847)	(33,198)	(36,806)	(63,010)	(169,861)	(42,172)	(60,000)	(60,000)	(60,000)	(222,172)	(120,000)	(155,000)
Acquisition, net	10,797	(20,766)	-	-	-	174	174	-	-	-	-	-	-	-
Dividends	(13,887)	(15,924)	(4,204)	(4,249)	(4,511)	(4,518)	(17,482)	(4,815)	(5,310)	(5,310)	(5,310)	(20,750)	(22,470)	(22,880)
Free CF	(11,808)	(74,432)	913	(5,351)	(33,217)	(46,343)	(83,998)	11,825	(35,070)	(55,740)	(40,940)	(119,932)	(4,790)	(29,090)
ST Borrowing (Repayments)	(16,513)	82,178	839	4,327	(26,545)	53,905	32,526	(11,125)	75,000	(35,000)	50,000	78,875	(98,000)	35,000
LTD Proceeds	49,975	-	-	-	-	-	-	-	-	70,000	-	70,000	100,000	-
LTD (Repaid)	(9,969)	(10,820)	(402)	(1,824)	(355)	(6,565)	(9,146)	(416)	(1,500)	(100)	(6,400)	(8,420)	(5,200)	(5,200)
Stock Issued	-	-	-	-	57,360	-	57,360	-	-	-	-	-	-	-
Issuance (Purchase) for DRIP	(165)	813	195	234	171	211	811	222	-	-	-	220	-	-
Net Cash Flow	11,520	(2,261)	1,545	(2,614)	(2,586)	1,208	(2,447)	506	38,430	(20,840)	2,660	20,743	(7,990)	710
EBITDA	\$95,476	\$107,730	\$43,883	\$23,522	\$18,365	\$30,486	\$116,255	\$43,488	\$24,140	\$23,150	\$37,470	\$128,260	\$153,030	\$166,810
EBITDA / GM	43.3%	45.0%	56.7%	40.7%	33.1%	43.5%	44.6%	51.7%	40.2%	37.3%	47.4%	44.9%	48.2%	49.4%
EV / TTM EBITDA	9.3x	9.5x	10.4x	10.5x	9.9x	10.7x	10.7x	10.9x	11.4x	12.0x	11.3x	11.3x	10.1x	9.3x
TTM-ROE	12.3%	12.4%	11.5%	11.6%	10.9%	11.2%	11.2%	10.4%	9.8%	9.8%	10.2%	10.2%	10.8%	10.5%

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.

Hilliard Lyons has received investment banking compensation from Chesapeake Utilities Corp. within the past 12 months.

Hilliard Lyons has acted as a manager or co-manager of an offering of securities of Chesapeake Utilities Corp. within the past 12 months.

### **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

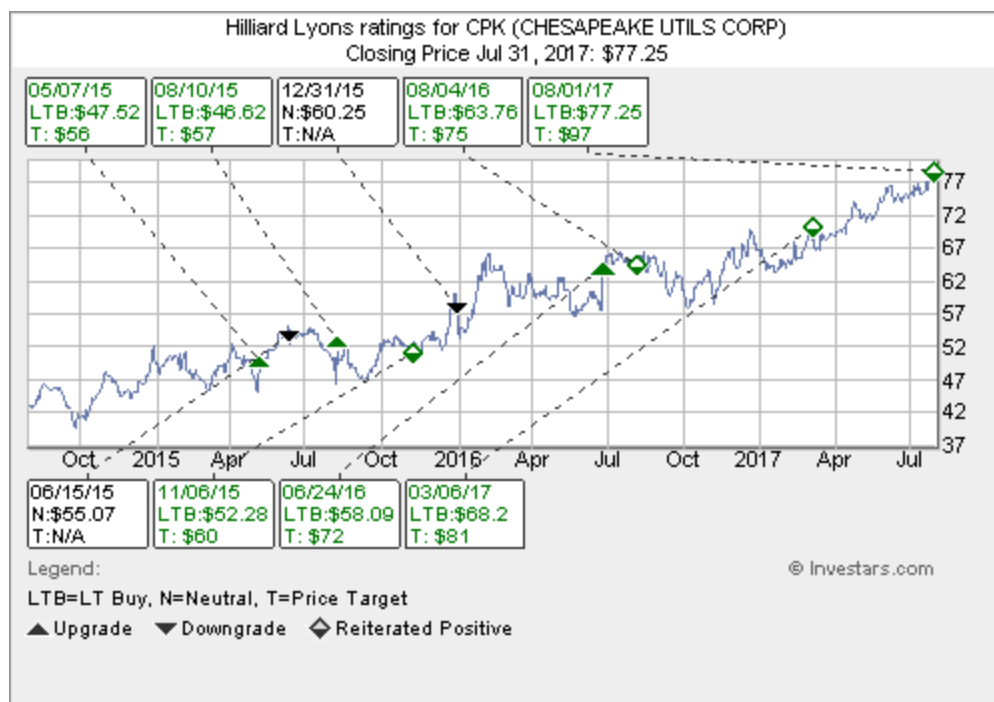
### **Investment Ratings**

**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	36	29%	14%	86%
Hold/Neutral	79	63%	5%	95%
Sell	10	8%	0%	100%

As of 7 July 2017

### Other Disclosures

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