

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

SJI - NYSE - as of	3/14/17	\$32.79
Price Target		\$40.00
52-Week Range	\$26.29 -	\$35.45
Shares Outstanding (mm)		79.3
Market Cap. (\$mm)		\$2,621.4
1-Mo. Average Daily Volume		315,159
Institutional Ownership		70.5%
Equity/Total Capital	Q4'16	49.1%
ROE	TTM	8.7%
Book Value / Share	Q4'16	\$16.19
Price / Book Value		2.0x
Dividend Yield		3.3%
LTM EBITDA Margin		30.3%

**Economic EPS (adjusted for mark-to-market) FY 12/31**

	Prior	Current	Prior	Current
2016A	2017E	2017E	2018E	2018E
1Q	\$0.80	\$0.73	\$0.73	--
2Q	*\$0.10	\$0.15	\$0.15	--
3Q	*\$0.01	\$0.03	\$0.04	--
4Q	\$0.42	\$0.58	\$0.57	--
Year	\$1.33	\$1.49	\$1.48	\$1.62
P/E	24.7x		22.2x	20.4x

\*HL-Adjusted for Special Items

**Utility Margin (\$MM)**

	Prior	Current	Prior	Current
2016A	2017E	2017E	2018E	2018E
1Q	\$109.9	--	\$118.4	--
2Q	\$43.6	--	\$47.3	--
3Q	\$31.9	--	\$34.9	--
4Q	\$79.0	--	\$85.6	--
Year	\$264.3	\$285	\$286.2	\$302

**Company Description:** *South Jersey Industries is an energy services holding company that provides a variety of products and services. It provides natural gas to 350,000+ customers in southern New Jersey, and sells natural gas to wholesale customers in the interstate market. Through its non-utility operations, the company markets energy services including natural gas, electricity, energy management, and consulting services, and own/operates a portfolio of solar power production.*

**Natural Gas Utilities**

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March 15, 2017

**South Jersey Industries, Inc.**

SJI – NYSE – Long-term Buy-3

**Upgrading Rating to Long-term Buy; \$40 Price Target.**

**Investment Highlights**

- We are upgrading our rating on SJI from Neutral to Long-term Buy; we assign shares a 2-year price target of \$40. Our suitability rating of '3' remains in place.
- Our timing is influenced by a ~6% month-to-date pullback in March, weakest amongst our coverage, and a desire to get ahead of the Fed decision this afternoon, such to prepare investors to capitalize on any potential near-term volatility/opportunity.
- Exiting 2016, we hold increased confidence in SJI's commitment to refining the business mix (emphasis on regulated ops) and plausibility of the '2020 plan.'
- SJI also flows in agreement with our rising appetite for owning a small slice of non-regulated operations (we particularly like the fuel supply business) that could benefit from tax reform without impacting valuation.
- Over our investment timeframe, we expect the narrative at South Jersey Gas can re-strengthen, representing a catalyst. We expect customer growth has troughed, new base rates should hit within the next two years, and BL England is finally moving forward.
- Improved profitability for legacy solar assets emerged in 2016, and in our view, represents a theme that is underappreciated into 2017. Having totally exited the development business, we see benefit from managing for maximum cash flow; higher SREC prices are converted to operating cash flow at a nearly 1:1 rate.
- Elimination of tax credit earnings (will occur this year) will improve earnings quality, in our view, decrease yr/yr volatility in results and produce cleaner quarters.
- At \$40, SJI shares would trade ~25x our 2018E EPS, which would value SJI in line with its 5-yr average 'high' TTM P/E. We view the story as strong as we can remember, and believe the stock is likely to reach former peak sentiment.

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

**ADDITIONAL DISCUSSION—MULTIPLE ITEMS**

Although perhaps counterintuitive for a gas utility, we actually believe the Utility segment may be underappreciated at this point. Customer growth around 1.2% is competitive versus the peer group, but in our view, has trended below SJI's long-term potential due to hardships in and around Atlantic City. Separately, we are in a slight vacuum as far as the regulatory calendar goes, in our view, with the 2014 base rate case having anniversaried, but the 2017 case (filed January 27) still relatively fresh to the narrative. Furthermore, the 2/24 approval for the BL England pipeline by the Pinelands Commission is still new to the story as well.

SJI stock has moved considerably higher from lows over the past year or two, but we believe the stock is underappreciated by the Street. Amongst eight sell side ratings, we mark just the second positive mention, which bolsters our case that sentiment still has room to improve (as implied by our price target).

**SUITABILITY**

We assign SJI a suitability rating of '3.' A complete description of our suitability scale is on page 5. Size versus the broad Utility sector and significant exposure to non-regulated and/or more cyclical market-based and renewable energy businesses keep SJI below our '2' suitability rating. Acceptable leverage ratios (following a recent secondary), a long history of capital return, and a strong core regulated utility franchise keep South Jersey Industries well above our most aggressive '4' rating.

**CONSIDERATIONS AND RISKS**

Utility operations are weather sensitive. Gas utilities face competition from alternative fuels. In the industrial market, customers have the capability of using natural gas or other fuels. Increases in gas prices can negatively impact the price benefits of natural gas to the end user.

Gas utilities are subject to regulation at the federal and state levels. Regulatory commissions can vary and have a significant bearing on the profitability of gas utilities. There are a number of items that can create volatility in the earnings results for the marketing segment, including weather, customer demand, supply/storage levels, gas price volatility, customer growth/retention, and accounting treatment.

SJI generates a significant portion of earnings via Investment Tax Credits (ITCs), which are subject to federal regulatory statutes. A change in laws regarding these credits may materially alter the reported financial performance of the company and/or the forward earnings outlook for the firm.

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

*Additional information is available upon request.*

South Jersey Industries, Inc.													
Income Statement (000s)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Operating Revenue:													
Utility	\$500,752	\$528,763	\$183,669	\$68,273	\$60,983	140,894	\$453,819					-	-
Nonutility	386,244	430,805	149,366	86,129	158,099	189,087	582,681	139,537	120,147	110,071	149,569	519,320	576,470
Total Operating Revenue	886,996	959,568	333,035	154,402	219,082	329,981	1,036,500						
Utility Margin								118,420	47,250	34,901	85,581	286,150	303,170
Operating Expenses:													
Cost of Gas -- Utility	230,093	239,763	65,206	19,508	25,353	57,087	167,154	-	-	-	-	-	-
Cost of Sales -- Non-Utility	306,859	319,579	87,769	78,832	117,635	129,597	413,833	114,420	98,520	90,260	97,220	400,420	435,580
Operations	140,260	148,672	38,797	36,250	34,796	42,114	151,957	17,960	17,900	20,310	27,610	83,780	91,380
Maintenance	13,457	16,183	4,384	4,259	4,150	4,756	17,549	2,610	3,780	3,140	4,280	13,810	14,760
Depreciation	63,004	72,451	20,701	22,296	23,109	24,283	90,389	22,190	23,990	24,880	26,720	97,780	106,780
Energy & Other Taxes	5,720	6,026	1,925	1,243	1,449	1,725	6,342	1,930	1,240	1,450	1,730	6,350	6,350
Total Operating Expense	759,393	802,674	218,782	162,388	206,492	259,562	847,224	159,110	145,430	140,040	157,560	602,140	654,850
Operating Income	127,603	156,894	114,253	(7,986)	12,590	70,419	189,276	98,847	21,967	4,932	77,590	203,330	224,790
Other Income / (Expense)	11,819	9,510	2,203	4,361	2,223	1,202	9,989	2,200	4,360	2,220	1,200	9,980	9,980
Interest Expense / (Income)	29,560	31,622	9,160	8,229	7,355	6,705	31,449	6,502	6,938	6,628	6,849	26,920	26,020
EBT	109,862	134,782	107,296	(11,854)	7,458	64,916	167,816	94,546	19,390	524	71,941	186,390	208,750
Income Tax / (Benefit)	4,449	1,360	39,267	(7,189)	2,807	19,266	54,151	36,370	7,560	200	26,560	70,690	81,410
Equity in Affiliated Co	(7,785)	(27,812)	158	(133)	5,013	358	5,396	83	(70)	2,632	188	2,830	1,490
Income from Cont'd Ops	\$97,628	\$105,610	\$68,187	(\$4,798)	\$9,664	\$46,008	\$119,061	\$58,259	\$11,760	\$2,956	\$45,569	\$118,530	\$128,830
Minus/plus:													
Unrlzd MTM Deriv (Gain) / Loss	4,500	(5,066)	(11,167)	22,523	(9,459)	(22,001)	(27,550)					-	-
Unrlzd Loss on PP&E	-	-	-	-	-	-	-					-	-
Other	(100)	(100)	(25)	(41)	(41)	(41)	(165)					-	-
Tax				(9,002)	3,816	8,538	10,813					-	-
Net Loss from Affil, not ongoing	-	-	-	-	-	-	-					-	-
Net Loss from Affil, ongoing	1,524	(1,524)	-	-	-	-	-					-	-
Rlzd (Gain) / Loss on inv hedges	427	54	2	23	(39)	696	683					-	-
Economic Earnings	\$103,979	\$98,974	\$56,997	\$8,705	\$3,941	\$33,200	\$102,842	\$58,259	\$11,760	\$2,956	\$45,569	\$118,530	\$128,830
EPS from Cont'd Ops	\$1.47		\$0.95	(\$0.06)	\$0.12	\$0.58							
Minus/plus:													
Unrealized MTM (gain)/loss	0.07	(0.07)	(0.16)	0.30	(0.12)	(0.28)	(0.25)					0.00	0.00
Tax				(0.12)	0.05	0.11	0.04						
Rlzd (gain)/loss on inv inject hedges	0.01	0.00	0.00	0.00	(0.00)	0.01	0.01					0.00	0.00
Economic EPS	\$1.57	\$1.43	\$0.80	\$0.12	\$0.05	\$0.42	\$1.38	\$0.73	\$0.15	\$0.04	\$0.57	\$1.48	\$1.61
Adjusted--Economic EPS		\$1.70		\$0.10	\$0.01		\$1.33						
Economic EPS -- ex-ITC (Adj if Nec)	\$1.11	\$1.14					\$1.21					\$1.48	\$1.61
Diluted Avg Shares	66,428	68,931	71,416	75,298	79,635	79,643	76,475	79,795	79,948	80,100	80,253	80,024	80,253
Dividends	\$0.960	\$1.018	\$0.264	\$0.264	\$0.264	\$0.273	\$1.064	\$0.273	\$0.273	\$0.273	\$0.28	\$1.101	\$1.145
<b>Rate of Change Analysis:</b>													
Utility Margin--Approx	9.2%	9.3%	4.3%	3.6%	3.3%	4.6%	4.1%	7.7%	8.5%	9.5%	8.3%	8.3%	5.9%
Operating Income	83.2%	23.0%	49.6%	-126.3%	nm	7.9%	20.6%	-13.5%	-375.1%	-60.8%	10.2%	7.4%	10.6%
Economic EPS--Adj if Necessary	3.7%	8.0%	-7.0%	-47.1%	nm	-41.3%	-21.8%	-8.5%	49.6%	-25.4%	36.2%	11.7%	8.3%
EBITDA	59.8%	20.3%	44.8%	-70.0%	959.6%	11.4%	21.9%	-10.3%	221.2%	-16.5%	10.1%	7.7%	10.1%
<b>Margin Analysis:</b>													
O + M / Utility GM	66.2%	65.0%	39.3%	93.0%	122.2%	59.3%	64.1%						
Op Income / Utility GM--Approx	54.9%	61.8%	104.0%	-18.3%	39.5%	89.1%	71.6%	83.5%	46.5%	14.1%	90.7%	71.1%	74.1%
Tax Rate	4.0%	1.0%	36.6%	60.6%	37.6%	29.7%	32.3%	38.5%	39.0%	38.1%	36.9%	37.9%	39.0%
* A portion of forward 'Operations Expense' is reflected in the Utility Margin projection	*\$30.3MM of ITC	*\$38.3MM of ITC	\$1.7MM in ITCs	\$1.1MM in ITCs **EEPS ajd for 1.3MM at gain	\$1.8MM in ITCs	\$4.5M in ITCs	*EEPS guide \$1.29-\$1.35 **\$9.1MM of ITC				initial PennEast; delayed	*modeling \$0MM of ITC	*modeling \$0.1M ITC

Source: Company reports and Hilliard Lyons estimates

## South Jersey Industries, Inc.

Balance Sheet Analysis (000s)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Cash	\$4,171	\$3,877	\$4,250	\$4,160	\$6,941	\$18,282	\$18,282	\$870	\$1,140	\$6,350	\$15,390	\$15,390	\$32,880
A/R	251,892	178,359	179,662	175,341	159,994	222,339	222,339	183,260	178,850	163,190	226,790	226,790	231,330
Natural Gas in Storage	63,246	54,211	38,571	44,499	50,787	53,857	53,857	39,340	45,390	51,800	54,930	54,930	56,030
Other CA	247,388	194,827	173,627	151,757	140,042	178,835	178,835	182,310	154,790	142,840	187,780	187,780	197,170
Total Current Assets	566,697	431,274	396,110	375,757	357,764	473,313	473,313	405,780	380,170	364,180	484,890	484,890	517,410
Net PP&E	2,134,103	2,448,105	2,478,166	2,514,890	2,547,107	2,623,770	2,623,770	2,666,580	2,707,590	2,802,710	2,875,990	2,875,990	3,119,210
Total Reg & Other Non-Current	505,901	520,970	546,601	556,429	568,428	590,918	590,918	578,420	565,920	553,420	540,920	540,920	440,920
Other	142,724	80,551	73,107	75,505	83,817	42,566	42,566	43,420	44,290	45,180	46,080	46,080	49,880
<b>Total Assets</b>	<b>3,349,425</b>	<b>3,480,900</b>	<b>3,493,984</b>	<b>3,522,581</b>	<b>3,557,116</b>	<b>3,730,567</b>	<b>3,730,567</b>	<b>3,694,200</b>	<b>3,697,970</b>	<b>3,765,490</b>	<b>3,947,880</b>	<b>3,947,880</b>	<b>4,127,420</b>
A/P	272,998	186,400	151,006	166,418	141,096	296,100	296,100	154,030	169,750	143,920	302,020	302,020	308,060
CP of LTD	149,909	29,454	28,604	244,605	231,909	231,909	231,909	231,000	231,000	230,000	30,000	30,000	300,000
N/P	245,700	431,700	339,500	145,400	230,200	296,100	296,100	301,100	126,100	226,100	301,100	301,100	331,100
Other CL	181,578	184,922	178,893	202,010	209,192	128,515	128,515	187,840	206,050	213,380	134,940	134,940	141,690
Total Current Liabilities	850,185	832,476	698,003	758,433	812,397	952,624	952,624	873,970	732,900	813,400	768,060	768,060	1,080,850
LTD	859,491	1,006,394	1,046,968	831,089	808,704	808,005	808,005	809,820	959,820	960,820	1,160,820	1,160,820	990,820
Def Inc Taxes	344,520	295,945	333,572	330,046	331,762	343,549	343,549	344,550	345,550	346,550	347,550	347,550	351,550
Other Liabilities	362,797	308,546	321,999	375,466	336,874	337,149	337,149	343,890	350,770	357,790	364,950	364,950	395,040
Shareholders' Equity	932,432	1,037,539	1,093,442	1,227,547	1,267,379	1,289,240	1,289,240	1,321,970	1,308,930	1,286,930	1,306,500	1,306,500	1,309,160
<b>Total Liab &amp; SE</b>	<b>3,349,425</b>	<b>3,480,900</b>	<b>3,493,984</b>	<b>3,522,581</b>	<b>3,557,116</b>	<b>3,730,567</b>	<b>3,730,567</b>	<b>3,694,200</b>	<b>3,697,970</b>	<b>3,765,490</b>	<b>3,947,880</b>	<b>3,947,880</b>	<b>4,127,420</b>
Cash Flow Analysis	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Net Income (Economic)	\$103,979	\$98,974	\$56,997	\$8,705	\$3,941	\$33,200	\$102,842	\$58,260	\$11,760	\$2,960	\$45,570	\$118,530	\$128,830
Depreciation	63,004	72,451	20,701	22,296	23,109	24,283	90,389	22,190	23,990	24,880	26,720	97,780	106,780
(Inc.) dec. in working cap.	(18,943)	51,875	(5,886)	58,792	2,634	(29,881)	25,659	(32,624)	59,810	2,700	(32,010)	(2,120)	(2,240)
Other Op	13,292	(36,506)	26,268	(29,774)	8,650	38,206	43,350	12,500	12,500	12,500	12,500	50,000	100,000
Operating CF	161,332	186,794	98,080	60,019	38,334	65,808	262,240	60,326	108,060	43,040	52,780	264,210	333,360
Cap Ex	(342,578)	(345,621)	(67,416)	(51,427)	(69,562)	(89,597)	(278,002)	(65,000)	(65,000)	(120,000)	(100,000)	(350,000)	(350,000)
Net Sale / (Purch) Rstd Inv	(22,337)	20,069	8,906	(1,125)	2,679	21,511	31,971	-	-	-	-	-	-
Other Inv	(10,104)	(45,100)	(737)	(3,312)	2,915	1,997	863	(1,000)	(1,000)	(1,000)	(1,000)	(4,000)	(4,000)
Investing CF	(375,019)	(370,652)	(59,247)	(55,864)	(63,968)	(66,089)	(245,168)	(66,000)	(66,000)	(121,000)	(101,000)	(354,000)	(354,000)
LTD Proceeds	329,000	130,000	61,000	-	-	-	61,000	-	150,000	31,000	-	181,000	130,000
LTD (Repay)	(21,000)	(125,009)	(12,905)	(173)	(35,379)	(909)	(49,366)	-	-	(31,000)	-	(31,000)	(30,000)
Net Borrow / (Repay) ST Facility	(108,200)	186,000	(92,200)	(194,100)	84,800	65,900	(135,600)	5,000	(175,000)	100,000	75,000	5,000	30,000
Stock Issued	80,680	63,192	5,645	208,818	(37)	-	214,426	5,000	5,000	5,000	5,000	20,000	0
Dividends	(63,869)	(70,158)	-	(18,790)	(20,962)	(42,628)	(82,380)	(21,740)	(21,790)	(21,830)	(22,740)	(88,100)	(91,870)
Other Fin	(2,571)	(461)	-	-	(7)	(10,740)	(10,747)	-	-	-	-	0	0
Financing CF	214,040	183,564	(38,460)	(4,245)	28,415	11,623	(2,667)	(11,740)	(41,790)	83,170	57,260	86,900	38,130
Net Cash Flow	353	(294)	373	(90)	2,781	11,342	14,405	(17,414)	270	5,210	9,040	(2,890)	17,490
FCF (including div)	(245,115)	(228,985)	30,664	(10,198)	(52,190)	(66,417)	(98,142)	(26,414)	21,270	(98,790)	(69,960)	(173,890)	(108,510)
EBITDA	190,607	229,345	134,954	14,310	35,699	94,702	279,665	121,037	45,957	29,812	104,310	301,110	331,570
EV / TTM EBITDA	14.9x	11.5x	11.3x	8.4x	11.7x	12.4x	12.4x	12.9x	12.0x	12.3x	12.5x	12.5x	10.8x
Selected Financial Statistics	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Book Value	\$13.83	\$14.90	\$15.31	\$16.30	\$15.91	\$16.19	\$16.19	\$16.57	\$16.37	\$16.07	\$16.28	\$16.28	\$16.31
Price / Book	2.1x	1.6x	1.9x	1.9x	1.9x	2.1x	2.1x	2.0x	2.0x	2.0x	2.0x	2.0x	2.0x
TTM earned-ROE	11.9%	10.2%	9.7%	10.8%	11.0%	8.7%	8.7%	8.4%	8.4%	8.2%	9.1%	9.1%	9.8%
Equity / Total Cap (inc ST & CP LTD)	42.6%	41.4%	43.6%	50.1%	49.9%	49.1%	49.1%	49.6%	49.8%	47.6%	46.7%	46.7%	44.7%
LT Debt / Total Cap	48.0%	49.2%	48.9%	40.4%	39.0%	38.5%	38.5%	38.0%	42.3%	42.7%	47.0%	47.0%	43.1%

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

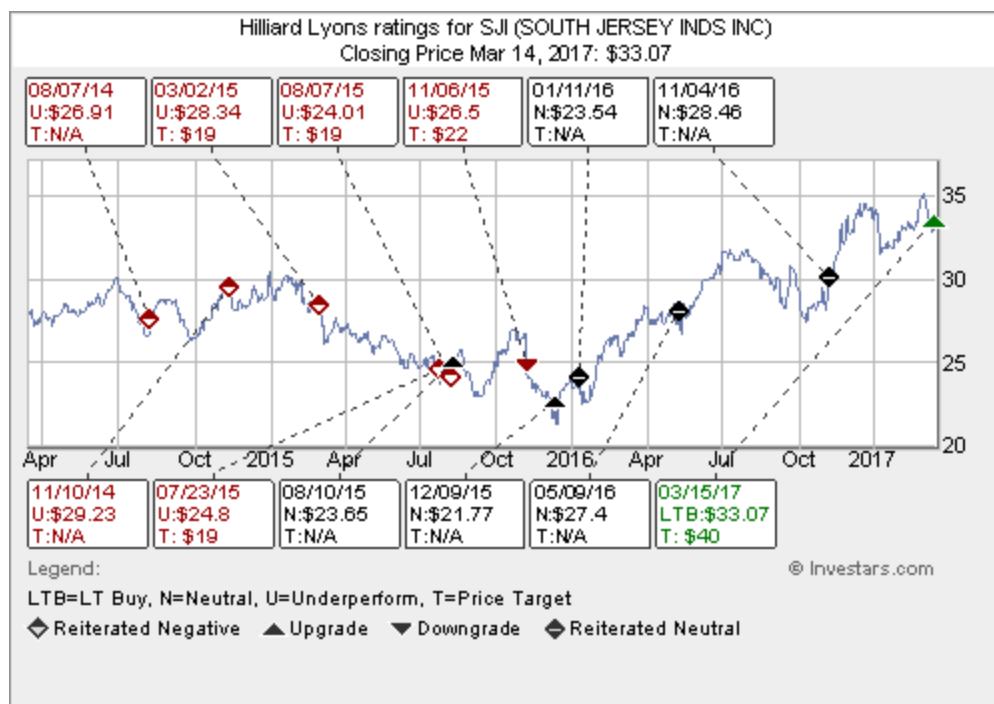
### **Investment Ratings**

**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	35	29%	14%	86%
Hold/Neutral	71	59%	6%	94%
Sell	15	12%	7%	93%

As of 8 March 2017

**Other Disclosures**

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