

Otter Tail Corporation  
A Financial Analysis and Valuation Report

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by

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## EXECUTIVE SUMMARY

Otter Tail Corporation is a holding company headquartered in Fergus Falls, MN with a business history of over 100 years. Their largest and longest-standing subsidiary is Otter Tail Power Company, but they also own four other subsidiaries branching out into the manufacturing and plastics industries as well. To better understand the current financial environment surrounding Otter Tail Corporation, I have gathered pertinent quantitative and qualitative data on the company from 2014-2018. As part of this research, I have also gathered the same data for another company to compare to within the same industry, also headquartered in the Midwest, and being similar in size. The company chosen for this benchmark process is Black Hills Corporation out of South Dakota. I used all of these findings to draw conclusions and make projections looking ahead to help provide the best recommendation to future investors.

I developed a valuation for my main corporation and was able to compare it to that of the current stock price as of the same period. From this, I found that the current selling price of the stock of Otter Tail Corporation was \$48.64 as of 12/31/2018. My valuation produced an estimated value of the stock as of the same date to be \$33.41. This shows the stock of Otter Tail Corporation to be currently traded at a price that is overvalued, and therefore I would recommend investors to sell their stock in Otter Tail Corporation.

## INTRODUCTION

Through this project, I have been tasked with gathering, preparing, and analyzing pertinent financial data to produce a justified buy, sell or hold recommendation on the common stock of Otter Tail Corporation. I am assuming the role of a financial analyst providing an in-depth analysis and valuation of Otter Tail Corporation's performance using a variety of measures, methods and tools. To successfully execute this, I had to first start with selecting a firm to analyze, Otter Tail Corporation, and then a benchmark firm that was comparable in the same region and industrial classification as the main firm.

The criteria by which my firms were selected was based on the following specifications; both firms were to be public companies that are headquartered or incorporated in the Midwest region, both firms were to be listed on the Russell 2000 Index for small cap firms, and both firms needed to have, at minimum, the same primary four-or three-digit Standard Industrial Classification Code (SIC). I first selected Otter Tail Corporation which is headquartered in Fergus Falls, MN, and in the electric utilities industry. Next, I selected Black Hills Corporation to use as my benchmark company, which is headquartered in Rapid City, SD and also a part of the electric utilities industry.

Once I had made my company selections, I gathered five years of financial statements and data for both my main and benchmark companies. At the start of my endeavor, the most recent financial data available was as of December 31, 2018 for both companies. I collected information from all the years ended going back to December 31, 2014. I was then able to compile this information to analyze sales growth, cost control, profitability, liquidity, asset turnover, capital structure, leverage, solvency, and cash management. I utilized the calculation of ratios and metrics to understand the financial

picture of Otter Tail Corporation, and also compare it to that of my benchmark, Black Hills Corporation using the same methods. Finally, I performed a valuation of my firm through forecasted annual future cash flows for the next five years. Through this valuation, I was able to form a conclusion as to whether Otter Tail Corporation is currently undervalued or overvalued, which led to my buy/hold/sell ultimate recommendation.

## **FIRM CHARACTERISTICS**

### **Overview**

Immediately upon my selection of Otter Tail Corporation, I was most aware of their business as Otter Tail Power Company. Though this is their most mature sector, with its start in 1907, this is just one venture held by the parent holding company that is now Otter Tail Corporation. The company began under the name Otter Tail Power Company from its inception in 1907, but ultimately changed its name to Otter Tail Corporation in 2001 to better represent the broader scope of services they would grow to provide. Soon after, Otter Tail Power Company transitioned from a branch of Otter Tail Corporation to a wholly owned subsidiary. This expansion continued, and as of December 2018, Otter Tail Corporation held five subsidiaries in the electric, manufacturing, and plastics industries.

### **Segments of Subsidiaries**

Otter Tail Power Company is an electric utility business operating out of its headquarters in Fergus Falls, MN. As previously mentioned, they have been in business since 1907 and currently employ 669 employees under the leadership of President Tim Rogelstad. Otter Tail Power Company provides energy and electric service to customers

in North Dakota, South Dakota, and Minnesota. Otter Tail Corporation holds two other subsidiaries in the manufacturing industry. These include BTD Manufacturing, Inc., a metal fabricator headquartered in Detroit Lakes, MN acquired in 1995. BTD employs 1,273 employees and is led by Paul Ginther. T.O. Plastics, Inc. is a custom plastic parts manufacturer acquired in 2001. T.O. Plastics is headquartered in Clearwater, MN and under the leadership of Mike Vallafskey, they currently employ 172 employees. Otter Tail Corporation's final two subsidiaries make up its share in the plastics industry. First is Northern Pipe Products, Inc. headquartered in Fargo, ND and acquired in 1995, which is a PVC pipe manufacturer with 100 employees led by Steve Laskey. Finally, Vinyltech Corporation, another PVC pipe manufacturer was acquired in 2000 and headquartered in Phoenix, AZ. This corporation is also under the direction of Steve Laskey and has 70 employees.

The electric segment is still the corporation's primary business segment, and its established footprint in the industry, especially in Minnesota and North Dakota has provided a great framework for the corporation to build upon. Maintaining this has helped to keep risk lowered with a proven, sturdy track record. Within Otter Tail's electric segment, they service commercial, residential, and industrial customers. In 2018, these categories were almost equally spread with 30-37% of total revenues for each category of customer. Though one customer did account for 11% of 2018's electric revenue, there are relatively few other large customers. This is also a positive as they are not reliant on just a few large players to sustain their earnings.

Another characteristic of the electric segment is the need to continued capital expenditures. There is a huge push toward more renewable resources. This need poses a

great impact on investments over at least the next five-year period. This is a heavy, but necessary undertaking that should be considered as we look at the future outlook of the electric segment. As of 2018, Otter Tail Power Company estimated that over the years 2019-2023, \$973 million will be invested for expanding, replacing and improving its electric facilities. This estimated amount includes \$348 million for a renewable wind and solar energy generation and conservation, \$150 million for the Astoria natural gas-fired generation plant, \$145 million for countless technology and infrastructure projects, as well as \$122 million for transmission assets.

Otter Tail Corporation's manufacturing segment includes contract machining, metal parts stamping, fabrication and painting, production of life science and industrial packaging, and more. Of the corporation's total consolidated operating revenue, 29% in 2018, 27% in 2017 and 28% in 2016 were from the manufacturing segment. The manufacturing segment faces intense competition from both domestic and foreign manufacturers. With competitors who are more established in their market, BTD Manufacturing and T.O. Plastics are continuing to push forward with high-performance products, innovation through their production, controlling costs through manufacturing techniques, expanding product offerings, and upholding close relationships and providing valuable support to its customers.

The plastics segment holds the smallest, yet still a significant, share of Otter Tail Corporation's consolidated revenue. Between the two subsidiaries, Otter Tail Corporation is represented through plants producing PVC pipes in Fargo, North Dakota and Phoenix, Arizona. These products are marketed through independent sales representatives, as well as company sales and customer service. The primary customer bases for this segment are



made up of wholesalers and distributors. Though no single customer in this segment account for over 10% of the consolidated revenue, two of their customers do make up 39% of the plastics segment revenue for 2018. One unique challenge in this particular segment is the costs associated with shipping being expensive. This leads competition to be mainly regional, rather than across the entire nation. Having a plant in Fargo allows Northern Pipe Products to service northern, midwestern, south-central and western regions in the United States, as well as central and western Canada. Vinyltech Corporation's plant in Phoenix allows service to the western, northwest and south-central regions in the United States.

### **Firm Strategy and Goals**

Otter Tail Corporation's primary goals looking ahead to 2019 and beyond are focused around intentional growth, focus on capital investment, continued improvement in operations, and talent development. The company plans to maintain a predictable stream of earnings by investing in opportunities that allow for rate base growth in its electric segment at Otter Tail Power Company. They will achieve this stable growth promise in their manufacturing and plastics divisions by investing in organic growth opportunities. Following this strategic focus, Otter Tail Corporation is confident this will maintain the company's credit quality and protect its ability to fund the dividend they promise their shareholders. Otter Tail Corporation prides themselves on the fact that they have paid dividends continuously since 1938. I will go into more specifics surrounding the dividend promise in a later section as this is a priority to Otter Tail Corporation, one that they intend to uphold as long as possible.

Based on these strategies and focus, Otter Tail Corporation has also laid out goals for growth and maintenance of the share of each segment of business they conduct. The company's goal is to deliver annual growth of between five to seven percent in earnings per share over the next several years, using the 2018 diluted earnings per share as their basis. Over the next years, Otter Tail Corporation anticipates the electric segment to make up 75-85% of its overall earnings, and the manufacturing and plastic segments to make up the remaining 15-25%.

### **2019 Business Outlook Electric Segment**

There are several positive impacts to net income for the electric segment looking ahead to 2019. The company expects a higher net income in 2019, as compared to the most recent information from 2018. One reason for this is due to the outcome of a rate case filed in South Dakota in 2018. Due to the heavy regulation of the electric segment, where the rates Otter Tail Power Company can charge is based off of applicable state regulations, this segment depends highly on this regulatory action. Interim rates were approved and implemented in October of 2018 for South Dakota, and we anticipate the final rates to be in line with the rates determined for the interim period. Another aspect of this to consider is that due to the Tax Cuts and Job Acts that prompted these changes, any negative impact to the South Dakota rates will be offset by lower tax rates owed. Additionally, Otter Tail Power Company also saw an increase in allowance for funds used during construction that will be used for planned capital projects. These projects include the Merricourt Wind Project and the Astoria Station, a power plant in South Dakota that will begin construction in 2019. Finally, a decrease in operating expenses due

to lower costs of pension (due to an increase in the discount rate), medical, workers compensation and retirement medical benefits.

There are also a couple potentially harmful impacts to keep in mind as we look ahead to business in 2019 for the electrical segment. The main factors for this would be an increase in property tax expense, as well as higher depreciation expenses due to all the capital expenditures being put into service in 2019. Another factor that will potentially offset some of the growth in net income from 2018 to 2019 is weather. Favorable weather in 2018 inflated earnings per share by about \$0.07 per share compared to a typical weather year. Depending on the weather outlook in 2019, this could decrease the growth from the prior year slightly.

### **2019 Business Outlook Manufacturing and Plastic Segment**

Otter Tail Corporation is also predicting an increase in net income from 2018 to 2019 in their manufacturing segment. One of the major components of this prediction is the backlog for the manufacturing companies. Going into 2019, there was a backlog of \$211 million, compared to the prior year where backlog was \$166 million. This is a positive in the sense that the demand is definitely there, but something these segments will have to keep an eye on to ensure they have proper capacity to fulfill these needs. Another contributor to this prediction is due to the increase in sales seen at Otter Tail's subsidiary, BTD. Most of this growth is organic, through BTD's existing customer base, and includes the recreation vehicle, lawn and garden, and agricultural end markets. The final major reason is due to the increased earnings year-over-year from the subsidiary, T.O. Plastics, who has seen continual growth in horticulture, life science and industrial markets.

The positive outlook for the manufacturing segment may be partially offset by a less optimistic prediction for the plastics segment moving into 2019. The rise in the prices of resin have impacted the operating margins for those subsidiaries. Though the company expects a higher volume of overall sales, the lower operating margins will likely contribute to a lower net income in 2019 than it experienced in 2018.

### **INDUSTRY CHARACTERISTICS**

To better understand the current environment of the electric industry in North America, I reviewed the industry profile releases from November 2017, May 2018 and November 2018. Though this data is representative of the entire United States as well as Canada, it still lays out a solid foundation to make better judgements given our financial findings at Otter Tail Corporation in the Midwest. The first industry segment I will discuss is the electric segment impacting Otter Tail Power Company.

During 2018, the electric industry in United States as a whole saw a progression of stronger performance compared with years prior. This was primarily caused by an increase in electricity use, but especially in the renewable category. The renewable sector continued to gain momentum thanks to the federal government's efforts towards new clean energy and environmental policies and regulations. Many utility companies have moved away from coal and instead moved to natural gas, wind, solar and other renewable sources that are continually being made cheaper as more supplies have grown available. Looking forward, industry experts worry that a lower consumption of electricity is on the horizon, posing a risk for limited utility earnings in some cases. This is an opportunity for Otter Tail Corporation to remain competitive by having the diversity that is brought about by their other business segments, manufacturing and plastics to overcome this time

The major players of the electric sector across the United States include leaders such as FirstEnergy Corp, Exelon Corp, American Electric Power Co., and NextEra Energy Inc. However, upon further research, none of these companies were headquartered or primarily servicing the Midwest. I dug deeper and found another competitor more comparable to the region Otter Tail Corporation services and found that Duke Energy was one of the largest electric power holding companies in the United States. Though they are headquartered in North Carolina, they service the Southeast and Midwest regions of the US.

Next, I will provide insight on the manufacturing segment covering both the manufacturing and plastic subsidiary industries. One of the major forces in the plastic and manufacturing industry is the continual threat of competition. This pressure is even larger with foreign players in the industry who are able to maintain lower costs such as wages and production. Many domestic competitors will also opt to move production offshore to combat these challenges. This is a huge factor that will continue to impact the manufacturing industry as a whole, as well as Otter Tail's subsidiaries in that segment.

### **Industry Risk Factors**

One of the major risk factors that Otter Tail Corporation is subjected to is due to the heavy amount of regulation on a federal, state and local level. Environmental laws and regulations related to air and water quality, waste management, natural resources and health safety can force potentially drastic changes to existing facilities and procedures causing a big risk relating to additional costs. Worse yet, if Otter Tail Corporation fails to comply with these regulations, they are vulnerable to potential criminal and civil penalty.

A common theme throughout this analysis is the reliance for the industries that Otter Tail Corporation is a participant in on solid financing options. These are important in both the short-term and long-term. Keeping up a solid credit rating, as well as access to reasonable borrowing rates has a large impact on the ability to continue to secure the necessary debt, as well as maintain the ability to repay these debts as needed.

Another risk that is generated from the addition of more subsidiaries in more recent years is the pressure for those subsidiaries to continue to perform. If the subsidiaries are unable to produce the sufficient earnings necessary, shareholders of the parent company are subject to negative impacts based on the inefficiency of just one or more sector.

## **HISTORICAL FINANCIAL STATEMENT ANALYSIS**

### **Summary of Significant Accounting Policies**

#### **Plant, Property, and Equipment**

Within the electric operations, Otter Tail's utility plant is stated at original cost. Contracted work, direct labor and materials, allocable overheads and allowance for funds used during construction are all included in cost of additions. In 2018, the amount of interest that was capitalized on the electric utility plant was \$1,206,000, compared to \$741,000 in 2017, and \$495,000 in 2016. Utility depreciation is calculated based on the straight-line method with a basis of the remaining estimated useful life. The useful lives of assets range from 5 to 82 years. Gains and losses on asset dispositions are accounted for in the accumulated provision for depreciation reserve. Retired property is charged to accumulated depreciation by taking the cost of property less salvage value.

For nonelectric operations, property and equipment is carried on the balance sheet at historical cost, or fair value if it was acquired as a part of a business combination. The property in these sectors are also depreciated using the straight-line method over the estimated useful life of each asset group. The assets in nonelectric operations have useful lives that range from 2 to 40 years. Contracted work, direct labor and materials, allocable overheads and capitalized interest is all included in the cost of additions. For the most recent three years, no interest was capitalized for nonelectric operations. Maintenance and repairs are expensed as they are incurred. When assets are disposed of, any gains or losses applicable to the dispositions are included in operating income.

As a whole, Otter Tail Corporation reviews its assets with a long useful life to determine whether any changes or circumstances show that the carrying amount of the assets are not recoverable. The company tests this impairment by comparing the carrying amount of the asset with net cash flows that are expected to be generated from the related assets. If it is determined that the net cash flows are lower than the carrying amount of the asset, Otter Tail Corporation will record an impairment loss for the difference.

### **Jointly Owned Facilities**

Otter Tail Power Company is a joint owner of two coal-fired steam-powered electric generation plants. The first plant is Big Stone Plant in Big Stone City, South Dakota, and the second plant is Coyote Station in Beulah, North Dakota. Otter Tail Power also has joint ownership in four large in-service transmission lines, as well as a fifth that is currently under construction. Otter Tail Power's share of the revenue and expenses of these jointly owned facilities are included in the consolidated statements of income. Below is a table that shows Otter Tail Power's percentage ownership in each, as

well as the amounts attributed to each category in the 2018 and 2017 consolidated balance sheets.

Jointly Owned Facilities (dollars in thousands)	OTP	Electric	Construction	Accumulated	Net Plant
	Ownership	Plant	Work in	Depreciation	
	Percentage	in Service	Progress		
<b>December 31, 2018</b>					
Big Stone Plant	53.9	% \$336,051	\$ 361	\$ (92,007 )	\$244,405
Coyote Station	35.0	% 177,713	2,588	(100,997 )	79,304
Fargo–Monticello 345 kV line	14.2	% 78,184	--	(5,891 )	72,293
Brookings–Southeast Twin Cities 345 kV line	4.8	% 26,281	--	(1,713 )	24,568
Bemidji–Grand Rapids 230 kV line	14.8	% 16,331	--	(2,091 )	14,240
Big Stone South–Brookings 345 kV line	50.0	% 53,235	(150 )	(1,264 )	51,821
Big Stone South–Ellendale 345 kV line <sup>1</sup>	50.0	% --	106,490	--	106,490
<b>December 31, 2017</b>					
Big Stone Plant	53.9	% \$329,942	\$ 1,074	\$ (74,165 )	\$256,851
Coyote Station	35.0	% 177,721	158	(103,944 )	73,935
Fargo–Monticello 345 kV line	14.2	% 78,192	--	(4,667 )	73,525
Brookings–Southeast Twin Cities 345 kV line	4.8	% 26,269	--	(1,293 )	24,976
Bemidji–Grand Rapids 230 kV line	14.8	% 16,331	--	(1,753 )	14,578
Big Stone South–Brookings 345 kV line	50.0	% 53,225	--	(434 )	52,791
Big Stone South–Ellendale 345 kV line <sup>1</sup>	50.0	% --	89,980	--	89,980
<sup>1</sup> Midcontinent Independent System Operator, Inc.					

## Revenue Recognition

The Financial Accounting Standards Board released a major update to the ASC, ASU 2014-09, Revenue from Contracts with Customers topic in May 2014. Otter Tail Corporation adopted these updates effective January 1, 2018, however, did not record a cumulative effect adjustment to retained earnings as this update had no material impact on the timing of revenue recognition for the company and its subsidiaries.

Otter Tail Corporation includes many diverse business operations which causes the need for several different methods they use to address revenue recognition. The recognition of revenue from contracts with customers depends on the product that is produced, or the service that is performed. Revenue will be recognized when the company has fulfilled its performance obligations as laid out under the contract and when it is probable that the amount owed to the company will be collected. Depending on the



product sold or the service performed, Otter Tail Corporation may recognize revenue over time in the case of delivery of electricity and related services or in the case of storage of a custom-made product.

### **Warranty Reserves**

Through their manufacturing and plastics subsidiaries, there are certain products which carry product warranties that last one year after the date of shipment. This includes post-sales support and repairs or replacement of a product at no additional charge to the customer for a specified period of time. All of the subsidiaries that are impacted by this do take in-depth measures to test product quality and processes to ensure that these costs are kept low. However, there are still some instances where these warranty reserves are necessary and important. Otter Tail Corporation estimates the amount to which is needed for the warranty reserves based on several factors. These include warranty terms, current and ongoing product failure rates, repair costs, product call rates, average cost per call, and current period product shipments. Though these measures are in place, neither the manufacturing or plastics segment have incurred significant warrant costs over at least the last three years.

### **Goodwill**

Otter Tail Corporation accounts for goodwill in accordance with the requirements set through ASC Topic 350, Intangibles-Goodwill and Other. The company tests for impairment of goodwill on an annual basis in the fourth quarter, and more as needed. They use both qualitative and quantitative assessments to determine the current fair value of goodwill and compares that to current book value to ensure book value doesn't exceed

the fair value. The table below illustrates changes to goodwill by business segment in both 2018 and 2017.

	Gross Balance	Accumulated Impairments	Balance (net of impairments) December 31, 2017	Adjustments to Goodwill in 2018	Balance (net of impairments) December 31, 2018
<i>(in thousands)</i>	December 31, 2017	Impairments	December 31, 2017	2018	December 31, 2018
Manufacturing	\$ 18,270	\$ --	\$ 18,270	\$ --	\$ 18,270
Plastics	19,302	--	19,302	--	19,302
Total	\$ 37,572	\$ --	\$ 37,572	\$ --	\$ 37,572

  

	Gross Balance	Accumulated Impairments	Balance (net of impairments) December 31, 2016	Adjustments to Goodwill in 2017	Balance (net of impairments) December 31, 2017
<i>(in thousands)</i>	December 31, 2016	Impairments	December 31, 2016	in 2017	December 31, 2017
Manufacturing	\$ 18,270	\$ --	\$ 18,270	\$ --	\$ 18,270
Plastics	19,302	--	19,302	--	19,302
Total	\$ 37,572	\$ --	\$ 37,572	\$ --	\$ 37,572

### Significant accounting policies – Black Hills Corporation

As mentioned in the introduction section, I will be using a similar sized company, also headquartered in the Midwest, to compare and contrast the financial information of Otter Tail Corporation to. The company I am using for this benchmark is Black Hills Corporation. Black Hills Corporation is a utility company headquartered in Rapid City, South Dakota. They are a holding company with a similar structure to Otter Tail Corporation, holding subsidiaries that span across a variety of business segments. The subsidiaries Black Hills Corporation hold include operations in electric utilities, gas utilities, power generation and mining. I have review the disclosures to their financial statements to address their significant accounting policies.

The first topic I will cover for Black Hills Corporation is how they handle revenue recognition. Black Hills Corporation recognizes revenue in accordance with GAAP and FASB standards by recognizing revenue in the amount that reflects the amount that they expect to receive in exchange for goods or services, at the time when control of goods and services are passed to their customers. Just as Otter Tail's subsidiary, Otter Tail Power, Black Hills is subjected to the same regulation dictating rates and charges to its customers.

The next consideration of the accounting procedures for Black Hills Corporation are their significant judgements and estimates in their financial statements. These include Tax Reform (Tax Cuts and Jobs Act) Revenue Reserve, Unbilled Revenue, Contract Balances, Practical Expedients, and Materials, Supplies and Fuel. Unbilled Revenue is a major component of their electrical segment as delivery of utilities often have occurred but a bill has not yet been issued to the customer. This amount is estimated based on several factors including previous balances and current prices for that jurisdiction. On a monthly basis, this amount is tied out to actual billing and accounted for in accounts receivable at its true value. The estimate necessary for materials, supplies and fuel is determining the value of these categories on the balance sheet. Black Hills uses the weighted-average cost method and values them at the lower-of-cost or net realizable value.

Finally, property, plant and equipment is handled by Black Hills in a very similar fashion to that of Otter Tail Corporation. Items included in property, plant and equipment are recorded at cost. They capitalize interest related to property, plant and equipment. Depreciation is calculated by taking the cost of such assets less the salvage value and

depreciating on a straight-line basis over the estimated service life of each class of property. An exception to this procedure is certain non-utility power plant components which are instead depreciated on a unit-of-production method based on plant hours run. Black Hills Corporation also has capitalized coal mining costs and coal leases, which they amortize on a unit-of-production method that is based on the volumes produced and estimated reserves.

### **Quality of Earnings**

#### **Audit Opinion**

Otter Tail Corporation uses Deloitte and Touche LLP as their external auditors. This accounting firm is based out of Minneapolis, Minnesota and has served as the company's auditor since 1944. Over the five-year period, Otter Tail Corporation received an audit opinion of Unqualified every year. It was the opinion of the auditors that the financial statements are presented fairly, in all material aspects. This opinion includes the financial position the company has presented, the results of its operations, and its cash flows in conformity with GAAP. The auditors then went on to say that it is their opinion that effective internal control over financial reporting was present, in all material aspects under the guidance established in Internal Control-Integrated Framework (2013) by COSO. The audits were in accordance with the standards of the PCAOB.

Black Hills Corporation also used Deloitte and Touche LLP out of Minneapolis, Minnesota as their external auditors. Deloitte and Touche have provided their auditing services to Black Hills Corporation since 2002. As with Otter Tail Corporation, the auditors performed the audits in accordance with PCAOB standards. Deloitte and Touche issued Black Hills Corporation an Unqualified opinion for all of the five years covered in

this report. In their audit report, Deloitte and Touche stated that it is their opinion that the financial position of Black Hills Corporation is presented fairly in all material aspects. They also expressed that appropriate internal control framework was in place at Black Hills Corporation that helped them to come up with this audit opinion. Based on the opinions from the external auditor for both my main company, Otter Tail Corporation, and the benchmark, Black Hills Corporation, I can conclude that the financial information I am provided through the financial statements are reliable, and indicative of high-quality earnings.

### Quality of Earnings Evaluation

Based on my analysis of the significant accounting policies and procedures, as well as the positive audit opinion for both companies, I believe the quality of earnings for both companies to be high. The next technique I used to test this is to compare annual operating income to annual net cash flows from operations. I performed this for both my main company, as well as the benchmark to interpret the outcome. For higher quality earnings to exist, the result of this test should produce an output close to one. The farther the fluctuation from one, whether positive or negative, indicates a lower quality of earnings. Included below is the results for this test for both the main company, Otter Tail Corporation, and the benchmark company, Black Hills Corporation.

<b>Otter Tail Corporation</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Operating Income</b>	\$ 129,389	\$ 132,287	\$ 116,631	\$ 109,214	\$ 99,531
<b>Net Cash Flows from Operations</b>	\$ 143,448	\$ 173,577	\$ 163,386	\$ 117,540	\$ 112,474
<b>Resultant</b>	0.9020	0.7621	0.7138	0.9292	0.8849

<b>Black Hills Corporation</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Operating Income</b>	\$ 397,037	\$ 416,736	\$ 336,181	\$ 29,795	\$ 263,868
<b>Net Cash Flows from Operations</b>	\$ 488,811	\$ 428,261	\$ 320,463	\$ 428,004	\$ 323,457
<b>Resultant</b>	0.8123	0.9731	1.0490	0.0696	0.8158

The main element that stood out to me immediately was the outlier of 2015 for my benchmark company. In 2015, Black Hills Corporation experienced a huge dip in their operating income. This was due to a combination of factors that was unique to 2015, rather than the operations of the company as a whole. A couple of the major items mentioned by Black Hills to explain this dramatic dip include an impairment charge to the crude oil and natural gas properties of \$158 million and third-party costs of an acquisition of SourceGas of about \$7 million. Because those are such specific circumstances, I moved on to look at the trends for each company over the five-year testing period. Otter Tail Corporation held an average resultant from the test of 0.8384. When I compare this to the benchmark company, including the 2015 year, Black Hill's resultant average was 0.7440. If I exclude the 2015 year, they held an average over the other four years of 0.9125. From this test it appears Otter Tail Corporation could do a better job of managing their cash flows from operations to be more in line with their operating income each year. Overall, Black Hills Corporation seems to be doing a better job upholding the quality of its earnings.

### **Liquidity**

My analysis continued with the history and trends laid out by both companies' financial statements. First, I looked at the current ratio for both my main company, as well as the benchmark. An ideal current ratio would fall somewhere between 1.2 to 2.0, to show that the company has double the liquid assets necessary to cover all the short-term liabilities. As of 2018, Otter Tail Corporation had a current ratio of 1.42. The trend for their current ratio has been headed in a positive direction as they were as low as 0.76 in 2015, meaning they did not have enough current assets to cover their current liabilities.

Over the next four-year period, this has steadily climbed back up to a much better position of 1.42 in 2018. The lower current ratio for Otter Tail Corporation was initially a concern to me, however they appear to be fairly in line with their competitors, as my benchmark company showed similar results. Further, Black Hills Corporation shows a negative trend to their current ratio as they were at nearly 2.0 in 2015, and currently sit at a 0.78. The industry that both companies are in do cause a great need for large amounts of debt carried on their books, especially with the push for more renewable energy options apparent in the five years this analysis covers. However, this is a potentially threat if they are not able to better adjust for this. It can impact not only their ability to repay debt, but also impact their ability to secure the financing needed from a financial institution to cover their growth and new projects.

The next liquidity aspect I analyzed was the acid test for both the main and benchmark. For the acid test, I am looking for an output of at least 1.0 to show the ability to repay liabilities. Additionally, I am looking at how inline the acid test is with their previously mentioned current ratios, as this can show that a company is relying too much on their inventory if there is a vast difference between the two outputs. To help illustrate my findings, I am including below a comparison showing the current ratios and acid tests for each of the five years in our sample for both the main and benchmark companies.

<b>Otter Tail Corporation</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Current Ratio</b>	1.42	0.93	0.96	0.76	1.28
<b>Acid Test</b>	0.45	0.33	0.32	0.23	0.30

  

<b>Black Hills Corporation</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Current Ratio</b>	0.78	0.88	0.88	1.98	0.70
<b>Acid Test</b>	0.45	0.41	0.52	1.45	0.32

The acid tests for both companies seem to be very in-line with each other when compared to their respective current ratios for each period. Though Otter Tail does fit into the

category of potentially relying too heavily on its inventory through its current ratio, the benchmark company follows that same pattern leading me to believe that might just be an aspect of their particular industries.

### **Profitability**

Next, I compared the current profitability ratio of net profit margin for both the main and benchmark firms. Due to the high costs associated with the industry both companies are in, I expected the net profit margins to be a bit lower than they may be in other industries. Upon some research, nationally, the utility and electric industry ranges from 4-11%. Otter Tail's net profit margin rose from 2014-2018 by almost 2% steadily to a current net profit margin in 2018 of 8.99%. Black Hills Corporation had a net profit margin of 15.94% in 2018, growing about 6.5% from 2014, outside of the dramatic outlier in 2015. Given this information, Otter Tail seems to be in line with national averages, but in our market have an opportunity to grow the net profit margin looking forward. One potential reason this difference exists is also due to the other subsidiaries Otter Tail holds, like their plastics segment who expressed through their note disclosures that the profit margin might suffer a bit due to resin prices increasing.

### **Sales Growth**

Both the main and benchmark companies experienced a drop in their sales from 2014 to 2015. Beginning in 2016, Otter Tail Corporation saw a steady increase in sales growth for the next three years. However, Black Hills Corporation interestingly had the opposite trend, with sales growth dropping significantly from 2016-2018. Shown in the table below, Black Hills Corporation experienced an impressive sales growth in 2016. This is partially offset by the dramatic loss in 2015 they were recovering from. I have



calculated the sales growth for each period given the five years of data and also the average of the periods to help determine the best predictor of sales growth moving forward.

	2018	2017	2016	2015	Average
<b>Sales Growth - Main</b>	7.90%	5.70%	3.04%	-2.43%	3.55%
<b>Sales Growth - Benchmark</b>	4.40%	9.19%	17.96%	-6.38%	6.29%

### **Cost Control**

Cost control is a particularly important aspect of the electric industry, as well as the manufacturing and plastics industries. With a smaller percentage of profit margin to work with, it is hugely important for both companies to manage their costs effectively.

### **Capital Structure**

Within their three industries, Otter Tail Corporation is reliant on debt to fund their operations and keep up with evolving projects. Otter Tail Corporation's debt ratio has continually stayed around 64-67%. The benchmark company, Black Hills Corporation has maintained a debt ratio of around similar figures, with a range of 67-73% over the five years included in the analysis. Otter Tail's ability to maintain a lower debt ratio than the benchmark figures is a positive sign that they will be able to continue to obtain the financing they need. Lenders will be calculating the credit worthiness of Otter Tail using this figure in conjunction with other factors. Keeping this ratio controlled is important for the health of the company moving forward.

### **Trend Analysis**

I performed a trend analysis for both Otter Tail Corporation as well as the benchmark company, Black Hills Corporation. This compares each figure of the income statement and balance sheet of each year to the first year of the analysis. This helps to

show a better picture of the overall trends for each aspect of the financial statements. A couple positive takeaways from the trend analysis of the main company was the growth in gross profit as well as operating income. However, when compared to the benchmark company, the growth of Otter Tail Corporation was significantly smaller, yet was steady and consistent. The growth of net income over the five-year period for the main company was about half that of the benchmark figures. The main and benchmark companies moved inversely to one another when it came to assets, as Otter Tail Corporation decreased its overall assets, and Black Hills Corporation increased its overall assets. The percentage change for both was fairly small though, so that didn't seem to be material in my analysis. The trend analysis also shed light on the ultimate decision on whether or not to invest as shareholders' equity did increase a steady amount for both companies, but yet again showed a much more significant spike in the benchmark's equity figures. This was expected after comparing the changes throughout the years on the income statements of both companies.

### **Historical Firm Analysis Connections to Industry and Market**

Otter Tail Corporation has moved fairly consistent with the characteristics of its industries. The most recent periods have seen a move towards renewable energy options. Otter Tail has been continuing to expand and strengthen its own renewable energy segments and options. They recognize this is the best strategy for them to stay competitive, but also to comply with the demands of regulations as they are set by the government. For the electricity sector, this is hand in hand with the market risk factors. The largest of which are currently the aggressive regulations faced in their industry, and the COVID-19 pandemic impacting the entire market across the globe. In order to

weather these two storms, they have to be diligent complying to these requirements and invest in the components necessary to get there. Given that their electricity is such an essential service, as long as they continue to keep up with current regulations, uphold their solid quality of earnings, and maintain the steady sales growth they have trended thus far, they will keep up with their history of proven success, even through the impacts of the pandemic.

The other industries that Otter Tail Corporation do business in, pose unique risks very different from the electric segment. On top of this, we must consider the relative newness of these subsidiaries when compared to the over 100 years of business the electric segment has. As I mentioned previously, a major risk factor impacting Otter Tail Corporation is the immense reliance on financing options to continue operations.

Through the historical financial analysis, I commented on the very high debt ratio Otter Tail holds. There is pressure on the subsidiaries to perform to the levels promised, and if not, the firm could lose its ability to repay those debts, as well as the ability to acquire the financing that will be definitely needed in the future. The risk factors of the market today and the characteristics of the electric, plastics, and manufacturing industries paired with the historical financial considerations analyzed before all play a huge part in the development of a fair valuation of the corporation.

## **VALUATION**

### **Assumptions Behind the Valuation**

To create a successful valuation model, there were several assumptions that I had to make to build a fairly presented financial picture behind the predictions. The first of these assumptions was related to sales growth. In the previous section, I discussed the

sales growth averages for Otter Tail Corporation, as well as for the benchmark company. I decided that combined with other differences between Otter Tail and Black Hills Corporation, my most appropriate estimate for starting growth was 10.0% and long-term sales growth was 3.0%. Not only is this figure in line with a five-year average for the company, but also in-line with projections and promises to shareholders by the executives of the company for annual growth.

The next assumption to consider was the WACC discount rate derivation. Many factors went into finding the appropriate WACC. This included the current stock price which I reflected as the most recent figure available of \$46.05 as of 04/06/2020 and the amount of common stock outstanding which was 200,788 shares. This calculation also took in historical financial figures, estimated cost of equity based on current beta of 0.43, risk-free rate of 4.85% and market risk premium of 9.92%. This calculation also included the company's credit rating which was found given the rating earned by Otter Tail Corporation using the S&P rating standards. Also included was the company's cost of debt capital which was found using the interest paid per year multiplied by (1-tax rate). Then, I calculated cost of short-term debt given the current tax rate and came up with a WACC value of 8.24% to be used in the valuation.

Otter Tail Corporation has done a fairly nice job of continuing with a steady and predictable trend over the five-year range of data that I have analyzed. In many of the historical financial factors that were discussed previously, any changes to non-cash working capital or even the change in fixed assets followed the average pattern and trend. For this reason, I have decided to keep the predictions for both of these figures in line with the averages based on historical data. As they continue to grow the manufacturing

and plastic subsidiaries, while continuing to expand electric operations, I believe we will see a continued trend for both of these two categories.

In performing this valuation, I have used the CAPM model. CAPM stands for Capital Asset Pricing Model. The CAPM model measures the expected return of an asset while considering risk factors in its industry and market. As mentioned before when explaining my WACC calculations, I calculated the expected return of investment given a few assumptions. The risk-free rate used in my model was based on the 10-year treasury bond average annual rate of 4.85%. The market rate of return I used was 9.92% based on the average annual return from the S&P 500 over the period of 1928-2019. From these figures, I found my equity risk premium to be 5.07%. The firm specific figure I used was the beta of Otter Tail Corporation, which I found given present data on Yahoo Finance. The formula for the CAPM model is shown below.

$$ER_i = R_f + \beta_i(ER_m - R_f)$$

**where:**

$ER_i$  = expected return of investment

$R_f$  = risk-free rate

$\beta_i$  = beta of the investment

$(ER_m - R_f)$  = market risk premium

### **Valuation Conclusions**

Using these assumptions, my annual forecasted free cash flows is estimated to grow fairly steadily beginning in 2023 at a rate of around 2.5-3.0% annually. My current

ROIC for 12/31/2018 was found to be 6.4%. Using my valuation model, the ROIC over the coming years will climb starting at about 5.5% and growing 1-2% from there each year. My valuation model predicted an estimated price per share as of 12/31/2018 to be \$33.41. I used this figure to compare to the current sales price of the common stock of Otter Tail Corporation that was traded as of 12/31/2018 at a price of \$48.64.

### **STOCK RECOMMENDATION**

Through my analysis of Otter Tail Corporation as whole, their subsidiaries and the unique factors that impact each of those sectors, current and past market and industry positions, as well as given the valuation results and historic financial analysis, I feel most comfortable with a recommendation to sell. While I do feel confident through my research that Otter Tail has made many smart decisions to maintain their footprint as a leader in the Midwest, while also branching out to expand and bring higher returns to their shareholders, I believe there is also a risk of an overvalued price per share given my valuation conclusions.

When comparing Otter Tail Corporation to the benchmark company, Black Hills Corporation, there were several instances where Otter Tail seemed to have the upper hand. However, there were also several categories in which they were behind their competitors. I believe a lot of this has to do with the new sectors of business that they have acquired and taken on with different business mixes compared to the utility sector they are most known for. Once I performed my valuation on the current stock value for Otter Tail, I came up with a value per share to be \$33.41. Comparing this to the current trading price as of 12/31/2018, at \$48.64, Otter Tail Corporation appears to be overvalued

by about \$15.00/share. Because of this disparity in value compared to trading price, I would recommend investors sell their stock currently held with Otter Tail.

## **APPENDIX A**



## CONSOLIDATED BALANCE SHEETS, DECEMBER 31

<i>(in thousands)</i>	2018	2017
<b>Assets</b>		
<b>Current Assets</b>		
Cash and Cash Equivalents	\$ 861	\$ 16,216
Accounts Receivable:		
Trade (less allowance for doubtful accounts of \$1,407 for 2018 and \$1,094 for 2017)	75,144	68,466
Other	9,741	7,761
Inventories	106,270	88,034
Unbilled Receivables	23,626	22,427
Income Taxes Receivable	2,439	1,181
Regulatory Assets	17,225	22,551
Other	6,114	12,491
<b>Total Current Assets</b>	<b>241,420</b>	<b>239,127</b>
<b>Investments</b>	<b>8,961</b>	<b>8,629</b>
<b>Other Assets</b>	<b>35,759</b>	<b>36,006</b>
<b>Goodwill</b>	<b>37,572</b>	<b>37,572</b>
<b>Other Intangibles-Net</b>	<b>12,450</b>	<b>13,765</b>
<b>Regulatory Assets</b>	<b>135,257</b>	<b>129,576</b>
<b>Plant</b>		
Electric Plant in Service	2,019,721	1,981,018
Nonelectric Operations	228,120	216,937
Construction Work in Progress	181,626	141,067
<b>Total Gross Plant</b>	<b>2,429,467</b>	<b>2,339,022</b>
Less Accumulated Depreciation and Amortization	848,369	799,419
<b>Net Plant</b>	<b>1,581,098</b>	<b>1,539,603</b>
<b>Total Assets</b>	<b>\$ 2,052,517</b>	<b>\$ 2,004,278</b>

See accompanying notes to consolidated financial statements.

## CONSOLIDATED BALANCE SHEETS, DECEMBER 31

(in thousands, except share data)

	2018	2017
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Short-Term Debt	\$ 18,599	\$ 112,371
Current Maturities of Long-Term Debt	172	186
Accounts Payable	96,291	84,677
Accrued Salaries and Wages	24,857	21,534
Accrued Taxes	17,287	16,808
Regulatory Liabilities	738	9,688
Other Accrued Liabilities	12,149	11,389
Total Current Liabilities	170,093	256,653
Pensions Benefit Liability	98,358	109,708
Other Postretirement Benefits Liability	71,561	69,774
Other Noncurrent Liabilities	24,326	22,769
<b>Commitments and Contingencies (note 9)</b>		
<b>Deferred Credits</b>		
Deferred Income Taxes	120,976	100,501
Deferred Tax Credits	19,974	21,379
Regulatory Liabilities	226,469	232,893
Other	1,895	3,329
Total Deferred Credits	369,314	358,102
<b>Capitalization (page 56)</b>		
Long-Term Debt—Net	590,002	490,380
Cumulative Preferred Shares—Authorized 1,500,000 Shares Without Par Value; Outstanding—None	—	—
Cumulative Preference Shares—Authorized 1,000,000 Shares Without Par Value; Outstanding—None	—	—
Common Shares, Par Value \$5 Per Share—Authorized, 50,000,000 Shares; Outstanding, 2018—39,664,884 Shares; 2017—39,557,491 Shares	198,324	197,787
Premium on Common Shares	344,250	343,450
Retained Earnings	190,433	161,286
Accumulated Other Comprehensive Loss	(4,144)	(5,631)
Total Common Equity	728,863	696,892
Total Capitalization	1,318,865	1,187,272
<b>Total Liabilities and Equity</b>	<b>\$2,052,517</b>	<b>\$2,004,278</b>

See accompanying notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF INCOME—FOR THE YEARS ENDED DECEMBER 31

<i>(in thousands, except per-share amounts)</i>	2018	2017	2016
<b>Operating Revenues</b>			
Electric			
Revenues from Contracts with Customers	\$ 450,637	\$ 436,477	\$ 425,245
Changes in Accrued Revenues under Alternative Revenue Programs	(439)	(1,971)	2,104
Total Electric	450,198	434,506	427,349
Product Sales from Contracts with Customers	466,249	414,844	376,190
Total Operating Revenues	916,447	849,350	803,539
<b>Operating Expenses</b>			
Production Fuel—Electric	66,815	59,690	54,792
Purchased Power—Electric System Use	68,355	64,807	63,226
Electric Operation and Maintenance Expenses	155,534	146,914	147,274
Cost of Products Sold (depreciation included below)	354,559	316,562	295,222
Other Nonelectric Expenses	51,544	41,492	38,683
Depreciation and Amortization	74,666	72,545	73,445
Property Taxes—Electric	15,585	15,053	14,266
Total Operating Expenses	787,058	717,063	686,908
Operating Income	129,389	132,287	116,631
Interest Charges	30,408	29,604	31,886
Nonservice Cost Components of Postretirement Benefits	5,509	5,620	5,110
Other Income	3,461	2,632	2,905
Income Before Income Taxes	96,933	99,695	82,540
Income Tax Expense	14,588	27,256	20,219
Net Income	\$ 82,345	\$ 72,439	\$ 62,321
Average Number of Common Shares Outstanding—Basic	39,600	39,457	38,546
Average Number of Common Shares Outstanding—Diluted	39,892	39,748	38,731
Basic Earnings Per Common Share	\$ 2.08	\$ 1.84	\$ 1.62
Diluted Earnings Per Common Share	\$ 2.06	\$ 1.82	\$ 1.61
Dividends Declared Per Common Share	\$ 1.34	\$ 1.28	\$ 1.25

See accompanying notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME—FOR THE YEARS ENDED DECEMBER 31

<i>(in thousands)</i>	<b>2018</b>	<b>2017</b>	<b>2016</b>
<b>Net Income</b>	<b>\$ 82,345</b>	<b>\$ 72,439</b>	<b>\$ 62,321</b>
<b>Other Comprehensive Income (Loss):</b>			
Unrealized Loss on Available-for-Sale Securities:			
Reversal of Previously Recognized Gains Realized on Sale of Investments and Included in Other Income During Period	<b>(105)</b>	(15)	(3)
(Losses) Gains Arising During Period	<b>(61)</b>	115	(14)
Income Tax Benefit (Expense)	<b>35</b>	(35)	6
Change in Unrealized Losses on Available-for-Sale Securities—net-of-tax	<b>(131)</b>	65	(11)
Pension and Postretirement Benefit Plans:			
Actuarial Gains (Losses) net of Regulatory Allocation Adjustment	<b>1,919</b>	(3,791)	(445)
Amortization of Unrecognized Postretirement Benefit Losses and Costs (note 11)	<b>985</b>	629	628
Income Tax (Expense) Benefit	<b>(755)</b>	1,266	(74)
Adjustment to Income Tax Expense Related to 2017 Tax Cuts and Jobs Act	<b>(531)</b>	—	—
Pension and Postretirement Benefit Plans—net-of-tax	<b>1,618</b>	(1,896)	109
<b>Total Other Comprehensive Income (Loss)</b>	<b>1,487</b>	(1,831)	98
<b>Total Comprehensive Income</b>	<b>\$ 83,832</b>	<b>\$ 70,608</b>	<b>\$ 62,419</b>

See accompanying notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDERS' EQUITY

<i>(in thousands, except common shares outstanding)</i>	Common Shares Outstanding	Par Value, Common Shares	Premium on Common Shares	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total Common Equity
<b>Balance, December 31, 2015</b>	<b>37,857,186</b>	<b>\$ 189,286</b>	<b>\$ 293,610</b>	<b>\$ 126,025</b>	<b>\$ (3,898)<sup>(a)</sup></b>	<b>\$ 605,023</b>
Common Stock Issuances, Net of Expenses	1,494,618	7,473	38,490			45,963
Common Stock Retirements and Forfeitures	(3,668)	(18)	(86)			(104)
Net Income				62,321		62,321
Other Comprehensive Income					98	98
Employee Stock Incentive Plan Expense			3,178			3,178
ASU 2016-09 Adoption			2,492	(623)		1,869
Common Dividends (\$1.25 per share)				(48,244)		(48,244)
<b>Balance, December 31, 2016</b>	<b>39,348,136</b>	<b>\$ 196,741</b>	<b>\$ 337,684</b>	<b>\$ 139,479</b>	<b>\$ (3,800)<sup>(a)</sup></b>	<b>\$ 670,104</b>
Common Stock Issuances, Net of Expenses	257,059	1,285	3,684			4,969
Common Stock Retirements and Forfeitures	(47,704)	(239)	(1,560)			(1,799)
Net Income				72,439		72,439
Other Comprehensive Income					(1,831)	(1,831)
Employee Stock Incentive Plan Expense			3,642			3,642
Common Dividends (\$1.28 per share)				(50,632)		(50,632)
<b>Balance, December 31, 2017</b>	<b>39,557,491</b>	<b>\$ 197,787</b>	<b>\$ 343,450</b>	<b>\$ 161,286</b>	<b>\$ (5,631)<sup>(a)</sup></b>	<b>\$ 696,892</b>
Common Stock Issuances, Net of Expenses	178,601	893	(986)			(93)
Common Stock Retirements and Forfeitures	(71,208)	(356)	(2,655)			(3,011)
Net Income				82,345		82,345
Other Comprehensive Income					1,487	1,487
Employee Stock Incentive Plan Expense			4,441			4,441
Common Dividends (\$1.34 per share)				(53,198)		(53,198)
<b>Balance, December 31, 2018</b>	<b>39,664,884</b>	<b>\$ 198,324</b>	<b>\$ 344,250</b>	<b>\$ 190,433</b>	<b>\$ (4,144)<sup>(a)</sup></b>	<b>\$ 728,863</b>

(a) Accumulated Other Comprehensive Loss on December 31 is comprised of the following:

<i>(in thousands)</i>	2018	2017	2016
Unrealized (Loss) Gain on Marketable Equity Securities:			
Before Tax	\$ (95)	\$ 71	\$ (29)
Tax Effect	20	(15)	10
Stranded Tax Effect	(10)	(10)	—
Unrealized (Loss) Gain on Marketable Equity Securities—net-of-tax	(85)	46	(19)
Unamortized Actuarial Losses and Prior Service Costs Related to Pension and Postretirement Benefits:			
Before Tax	(6,558)	(9,462)	(6,300)
Tax Effect	1,705	2,991	2,519
Stranded Tax Effect	794	794	—
Unamortized Actuarial Losses and Prior Service Costs Related to Pension and Postretirement Benefits—net-of-tax	(4,059)	(5,677)	(3,781)
Accumulated Other Comprehensive Loss:			
Before Tax	(6,653)	(9,391)	(6,329)
Tax Effect	1,725	2,976	2,529
Stranded Tax Effect	784	784	—
Net Accumulated Other Comprehensive Loss	\$ (4,144)	\$ (5,631)	\$ (3,800)

See accompanying notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CASH FLOWS—FOR THE YEARS ENDED DECEMBER 31

<i>(in thousands)</i>	2018	2017	2016
<b>Cash Flows from Operating Activities</b>			
Net Income	\$ 82,345	\$ 72,439	\$ 62,321
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Depreciation and Amortization	74,666	72,545	73,445
Deferred Tax Credits	(1,405)	(1,470)	(1,657)
Deferred Income Taxes	19,224	24,001	19,124
Change in Deferred Debits and Other Assets	941	(2,173)	(10,090)
Discretionary Contribution to Pension Plan	(20,000)	—	(10,000)
Change in Noncurrent Liabilities and Deferred Credits	(2,414)	19,257	14,685
Allowance for Equity/Other Funds Used During Construction	(2,194)	(986)	(857)
Stock Compensation Expense—Equity Awards	4,441	3,642	3,178
Other—Net	—	10	7
Cash (Used for) Provided by Current Assets and Current Liabilities:			
Change in Receivables	(8,559)	(2,135)	(944)
Change in Inventories	(18,236)	(4,294)	1,874
Change in Other Current Assets	(754)	(3,060)	(2,541)
Change in Payables and Other Current Liabilities	14,997	(3,013)	11,502
Change in Interest Payable and Income Taxes Receivable/Payable	396	(1,186)	3,339
<b>Net Cash Provided by Operating Activities</b>	<b>143,448</b>	<b>173,577</b>	<b>163,386</b>
<b>Cash Flows from Investing Activities</b>			
Capital Expenditures	(105,425)	(132,913)	(161,259)
Proceeds from Disposal of Noncurrent Assets	2,378	4,491	4,837
Acquisition Purchase Price Cash Received	—	—	1,500
Cash Used for Investments and Other Assets	(4,372)	(4,168)	(4,402)
<b>Net Cash Used in Investing Activities</b>	<b>(107,419)</b>	<b>(132,590)</b>	<b>(159,324)</b>
<b>Cash Flows from Financing Activities</b>			
Change in Checks Written in Excess of Cash	(345)	2,434	(3,363)
Net Short-Term (Repayments) Borrowings	(93,772)	69,488	(37,789)
Proceeds from Issuance of Common Stock	—	4,349	44,435
Common Stock Issuance Expenses	(108)	—	(562)
Payments for Retirement of Capital Stock	(3,011)	(1,799)	(104)
Proceeds from Issuance of Long-Term Debt	100,000	—	130,000
Short-Term and Long-Term Debt Issuance Expenses	(761)	(380)	(888)
Payments for Retirement of Long-Term Debt	(189)	(48,231)	(87,547)
Dividends Paid and Other Distributions	(53,198)	(50,632)	(48,244)
<b>Net Cash Used in Financing Activities</b>	<b>(51,384)</b>	<b>(24,771)</b>	<b>(4,062)</b>
<b>Net Change in Cash and Cash Equivalents</b>	<b>(15,355)</b>	<b>16,216</b>	<b>—</b>
<b>Cash and Cash Equivalents at Beginning of Period</b>	<b>16,216</b>	<b>—</b>	<b>—</b>
<b>Cash and Cash Equivalents at End of Period</b>	<b>\$ 861</b>	<b>\$ 16,216</b>	<b>\$ —</b>

See accompanying notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CAPITALIZATION, DECEMBER 31

<i>(in thousands)</i>	2018	2017
<b>Short-Term Debt</b>		
Otter Tail Corporation Credit Agreement	\$ 9,215	\$ —
Otter Tail Power Company Credit Agreement	9,384	112,371
<b>Total Short-Term Debt</b>	<b>\$ 18,599</b>	<b>\$ 112,371</b>
<b>Long-Term Debt</b>		
<b>Obligations of Otter Tail Corporation</b>		
3.55% Guaranteed Senior Notes, due December 15, 2026	\$ 80,000	\$ 80,000
North Dakota Development Note, 3.95%, due April 1, 2018	—	27
Partnership in Assisting Community Expansion (PACE) Note, 2.54%, due March 18, 2021	523	684
<b>Total—Otter Tail Corporation</b>	<b>80,523</b>	<b>80,711</b>
Less: Current Maturities—net of Unamortized Debt Issuance Costs	172	186
Unamortized Long-Term Debt Issuance Costs	407	461
<b>Total Otter Tail Corporation Long-Term Debt net of Unamortized Debt Issuance Costs</b>	<b>79,944</b>	<b>80,064</b>
<b>Obligations of Otter Tail Power Company</b>		
Senior Unsecured Notes 4.63%, due December 1, 2021	140,000	140,000
Senior Unsecured Notes 6.15%, Series B, due August 20, 2022	30,000	30,000
Senior Unsecured Notes 6.37%, Series C, due August 20, 2027	42,000	42,000
Senior Unsecured Notes 4.68%, Series A, due February 27, 2029	60,000	60,000
Senior Unsecured Notes 6.47%, Series D, due August 20, 2037	50,000	50,000
Senior Unsecured Notes 5.47%, Series B, due February 27, 2044	90,000	90,000
Senior Unsecured Notes 4.07%, Series 2018A, due February 7, 2048	100,000	—
<b>Total—Otter Tail Power Company</b>	<b>512,000</b>	<b>412,000</b>
Less: Current Maturities—net of Unamortized Debt Issuance Costs	—	—
Unamortized Long-Term Debt Issuance Costs	1,942	1,684
<b>Total Otter Tail Power Company Long-Term Debt net of Unamortized Debt Issuance Costs</b>	<b>510,058</b>	<b>410,316</b>
<b>Total Consolidated Long-Term Debt</b>	<b>592,523</b>	<b>492,711</b>
Less: Current Maturities—net of Unamortized Debt Issuance Costs	172	186
Unamortized Long-Term Debt Issuance Costs	2,349	2,145
<b>Total Consolidated Long-Term Debt net of Unamortized Debt Issuance Costs</b>	<b>590,002</b>	<b>490,380</b>
<b>Cumulative Preferred Shares—Without Par Value, Authorized 1,500,000 Shares; Outstanding: None</b>		
<b>Cumulative Preference Shares—Without Par Value, Authorized 1,000,000 Shares; Outstanding: None</b>		
<b>Total Common Shareholders' Equity</b>	<b>728,863</b>	<b>696,892</b>
<b>Total Capitalization</b>	<b>\$ 1,318,865</b>	<b>\$ 1,187,272</b>

See accompanying notes to consolidated financial statements.

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5)

Balance Sheet (1-5)

**Vertical Analysis**

**MAIN**

**Courtney**

**2018**

5

5

INCOME STATEMENT	2018	2017	2016	2015	2014
Net Sales	100.00%	100.00%	100.00%	100.00%	100.00%
Less: Cost of Goods Sold	38.69%	37.27%	36.74%	37.83%	38.54%
Gross Profit	61.31%	62.73%	63.26%	62.17%	61.46%
Other Operating Revenue	0.00%	0.00%	0.00%	0.00%	0.00%
Less: Operating Expenses	47.19%	47.15%	48.75%	48.16%	49.00%
Operating Income	14.12%	15.58%	14.51%	14.01%	12.45%
Less: Interest Expense (no capitalized interest)	3.32%	3.49%	3.97%	4.00%	3.71%
Other Income (Expenses)	-0.22%	-0.35%	-0.27%	0.28%	0.45%
Unusual or Infreq. Item; Gain (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
Equity in Earnings of Assoc. ; Profit (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
Income before Taxes	10.58%	11.74%	10.27%	10.29%	9.19%
Less:Taxes Related to Operations	1.59%	3.21%	2.52%	2.78%	2.07%
N.I. before Min. Ern.	8.99%	8.53%	7.76%	7.51%	7.12%
Minority Share of Earnings (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
N.I. before Nonrecurring Items	8.99%	8.53%	7.76%	7.51%	7.12%



Oper. of Discontinued Segment;					
Income (Loss)	0.00%	0.00%	0.00%	-0.69%	0.81%
Disposal of Discont. Segment;					
Gain (Loss)	0.00%	0.00%	0.00%	0.92%	0.00%
Extraordinary Item;					
Gain (Loss)	0.16%	-0.22%	0.01%	-0.13%	-0.70%
Cum. Effect of Acct Change;					
Gain (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
	-----	-----	-----	-----	-----
Net Income (Loss)	9.15%	8.31%	7.77%	7.61%	7.22%
=====	=====	=====	=====	=====	=====

BALANCE SHEET	2018	2017	2016	2015	2014
<b>ASSETS</b>					
Current Assets:					
Cash	0.04%	0.81%	0.00%	0.00%	0.00%
Marketable Securities	0.00%	0.00%	0.00%	0.00%	0.00%
Gross Receivables	3.73%	3.47%	3.63%	3.53%	3.52%
Less: Allowance for Bad Debts	0.07%	0.05%	0.07%	0.07%	0.06%
Net Trade Receivables	3.66%	3.42%	3.57%	3.46%	3.46%
Inventories	5.18%	4.39%	4.38%	4.69%	4.89%
Prepaid Expenses	0.00%	0.00%	0.00%	0.00%	0.00%
Other Current Assets	2.88%	3.31%	2.93%	3.20%	6.39%
Total Current Assets	11.76%	11.93%	10.88%	11.35%	14.74%
Long-Term Assets:					
Net Tangible (Fixed) Assets (other than construction in progress)	68.18%	69.78%	69.23%	71.84%	58.59%
Construction in Progress	8.85%	7.04%	8.01%	4.37%	14.29%
Intangible Assets	0.61%	0.69%	0.78%	0.86%	0.65%
Investments	0.44%	0.43%	0.44%	0.45%	0.49%
Other Nonoperating Assets	8.42%	8.34%	8.87%	9.20%	9.27%
Other Operating Assets	1.74%	1.80%	1.78%	1.92%	1.98%
Total Long-Term Assets	88.24%	88.07%	89.12%	88.65%	85.26%
Total Assets	100.00%	100.00%	100.00%	100.00%	100.00%
<b>LIABILITIES AND EQUITY</b>					
Current Liabilities:					
Accounts Payable	4.69%	4.22%	4.67%	4.92%	6.15%
Short Term Loans	0.91%	5.61%	2.24%	4.43%	0.62%
Current Maturity of L.t. Debt	0.01%	0.01%	1.74%	2.89%	0.01%
Other Current Liabilities	2.68%	2.96%	2.63%	2.66%	4.74%
Total Current Liabilities	8.29%	12.81%	11.28%	14.90%	11.52%
Long-Term Liabilities:					
Long-term Debt	28.75%	24.47%	26.42%	24.49%	28.64%
Reserves	0.00%	0.00%	0.00%	0.00%	0.00%
Deferred Liabilities	0.00%	0.00%	0.00%	0.00%	0.00%
Minority Interest	0.00%	0.00%	0.00%	0.00%	0.00%
Redeemable Preferred	0.00%	0.00%	0.00%	0.00%	0.00%

Other Long-term Liabilities	27.46%	27.96%	27.26%	27.39%	26.93%
	-----	-----	-----	-----	-----
Total Long-term Liabilities	56.20%	52.42%	53.68%	51.88%	55.57%
Total Liabilities	64.49%	65.23%	64.96%	66.77%	67.10%
Shareholders' Equity:					
Preferred Equity	0.00%	0.00%	0.00%	0.00%	0.00%
Common Equity-incl. Ret. Ern.	35.51%	34.77%	35.04%	33.23%	32.90%
	-----	-----	-----	-----	-----
Total Equity	35.51%	34.77%	35.04%	33.23%	32.90%
Total Liabilities and Equity	100.00%	100.00%	100.00%	100.00%	100.00%
=====	=====	=====	=====	=====	=====

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5) 5

Balance Sheet (1-5) 5

**Horizontal Analysis**

**MAIN**

**Courtney**

**2018**

INCOME STATEMENT	2018	2017	2016	2015	2014
Net Sales	114.66%	106.27%	100.54%	97.57%	100.00%
Less: Cost of Goods Sold	115.09%	102.76%	95.83%	95.77%	100.00%
Gross Profit	114.39%	108.47%	103.49%	98.69%	100.00%
Other Operating Revenue	#N/A	#N/A	#N/A	#N/A	#N/A
Less: Operating Expenses	110.43%	102.26%	100.01%	95.89%	100.00%
Operating Income	130.00%	132.91%	117.18%	109.73%	100.00%
Less: Interest Expense (no capitalized interest)	102.56%	99.85%	107.55%	105.10%	100.00%
Other Income (Expenses)	-57.58%	-84.00%	-61.99%	61.20%	100.00%
Unusual or Infreq. Item; Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Equity in Earnings of Assoc. ; Profit (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Income before Taxes	131.99%	135.75%	112.39%	109.25%	100.00%
Less:Taxes Related to Operations	88.11%	164.62%	122.12%	130.71%	100.00%
N.I. before Min. Ern.	144.76%	127.35%	109.56%	103.00%	100.00%
Minority Share of Earnings (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A

N.I. before Nonrecurring Items	144.76%	127.35%	109.56%	103.00%	100.00%
Oper. of Discontinued Segment;					
Income (Loss)	0.00%	0.00%	0.00%	-83.85%	100.00%
Disposal of Discont. Segment;					
Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Extraordinary Item;					
Gain (Loss)	-26.53%	32.67%	-1.75%	17.84%	100.00%
Cum. Effect of Acct Change;					
Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Net Income (Loss)	145.23%	122.32%	108.14%	102.81%	100.00%

BALANCE SHEET	2018	2017	2016	2015	2014
<b>ASSETS</b>					
Current Assets:					
Cash	#N/A	#N/A	#N/A	#N/A	#N/A
Marketable Securities	#N/A	#N/A	#N/A	#N/A	#N/A
Gross Receivables	125.04%	113.62%	113.51%	104.93%	100.00%
Less: Allowance for Bad Debts	134.26%	104.39%	118.89%	120.42%	100.00%
Net Trade Receivables	124.88%	113.78%	113.41%	104.66%	100.00%
Inventories	124.73%	103.32%	98.28%	100.25%	100.00%
Prepaid Expenses	#N/A	#N/A	#N/A	#N/A	#N/A
Other Current Assets	53.19%	59.73%	50.39%	52.43%	100.00%
<b>Total Current Assets</b>	<b>94.10%</b>	<b>93.20%</b>	<b>81.08%</b>	<b>80.56%</b>	<b>100.00%</b>
Long-Term Assets:					
Net Tangible (Fixed) Assets (other than construction in progress)	137.22%	137.13%	129.82%	128.27%	100.00%
Construction in Progress	73.04%	56.73%	61.63%	32.01%	100.00%
Intangible Assets	110.66%	122.34%	132.95%	139.30%	100.00%
Investments	104.42%	100.55%	98.08%	96.53%	100.00%
Other Nonoperating Assets	107.11%	103.59%	105.15%	103.77%	100.00%
Other Operating Assets	103.92%	104.64%	99.11%	101.73%	100.00%
<b>Total Long-Term Assets</b>	<b>122.03%</b>	<b>118.94%</b>	<b>114.84%</b>	<b>108.77%</b>	<b>100.00%</b>
<b>Total Assets</b>	<b>117.91%</b>	<b>115.14%</b>	<b>109.86%</b>	<b>104.61%</b>	<b>100.00%</b>
<b>LIABILITIES AND EQUITY</b>					
Current Liabilities:					
Accounts Payable	89.98%	79.13%	83.49%	83.63%	100.00%
Short Term Loans	171.36%	1035.30%	395.09%	743.25%	100.00%
Current Maturity of L.t. Debt	85.57%	92.54%	16517.91%	26141.29%	100.00%
Other Current Liabilities	66.68%	71.99%	60.87%	58.79%	100.00%
<b>Total Current Liabilities</b>	<b>84.79%</b>	<b>127.94%</b>	<b>107.51%</b>	<b>135.21%</b>	<b>100.00%</b>
Long-Term Liabilities:					
Long-term Debt	118.36%	98.37%	101.37%	89.46%	100.00%
Reserves	#N/A	#N/A	#N/A	#N/A	#N/A

Deferred Liabilities	#N/A	#N/A	#N/A	#N/A	#N/A
Minority Interest	#N/A	#N/A	#N/A	#N/A	#N/A
Redeemable Preferred	#N/A	#N/A	#N/A	#N/A	#N/A
Other Long-term Liabilities	120.20%	119.52%	111.18%	106.37%	100.00%
-----					
Total Long-term Liabilities	119.25%	108.62%	106.13%	97.65%	100.00%
Total Liabilities	113.33%	111.94%	106.37%	104.11%	100.00%
Shareholders' Equity:					
Preferred Equity	#N/A	#N/A	#N/A	#N/A	#N/A
Common Equity-incl. Ret. Ern.	127.25%	121.67%	116.99%	105.63%	100.00%
-----					
Total Equity	127.25%	121.67%	116.99%	105.63%	100.00%
Total Liabilities and Equity	117.91%	115.14%	109.86%	104.61%	100.00%
=====					

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5)

Balance Sheet (1-5)

**Ratios - average**

**MAIN**

**Courtney**

**2018**

5

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LIQUIDITY	2018	2017	2016	2015	2014
Days' Sales in Receivables	30.49	29.89	31.56	30.07	27.96
Accounts Receivable Turnover	12.54	12.22	12.02	12.43	
A/R Turnover in Days	29.10	29.88	30.37	29.36	
Days' Sales in Inventory	109.40	101.50	103.53	105.67	100.95
Inventory Turnover	3.65	3.69	3.49	3.46	
Inventory Turnover in Days	100.01	99.03	104.57	105.54	
Operating Cycle	129.11	128.91	134.94	134.90	
Working Capital	71,327	(17,526)	(7,656)	(64,549)	55,968
Current Ratio	1.42	0.93	0.96	0.76	1.28
Acid Test	0.45	0.33	0.32	0.23	0.30
Cash Ratio	0.01	0.06	0.00	0.00	0.00
Sales to Working Capital	34.07	-67.46	-22.26	-181.75	
Cash Flow/Cur. Mat. of Debt & NP	0.00	0.00	0.00	0.00	0.00
LONG-TERM DEBT-PAYING ABILITY	2018	2017	2016	2015	2014
Times Interest Earned	4.19	4.37	3.59	3.57	3.48
Fixed Charge Coverage	4.19	4.37	3.59	3.57	3.48
Debt Ratio	64.49%	65.23%	64.96%	66.77%	67.10%
Debt/Equity	181.61%	187.60%	185.39%	200.96%	203.91%
Debt to Tangible Net Worth	184.76%	191.38%	189.62%	206.31%	208.00%
Cash Flow/Total Debt	0.00%	0.00%	0.00%	0.00%	0.00%



PROFITABILITY	2018	2017	2016	2015	2014
Net Profit Margin	8.99%	8.53%	7.76%	7.51%	7.12%
Total Asset Turnover	0.45	0.43	0.43	0.44	
Return on Assets	4.06%	3.70%	3.34%	3.29%	
Operating Income Margin	14.12%	15.58%	14.51%	14.01%	12.45%
Operating Asset Turnover	0.55	0.52	0.52	0.55	
Return on Operating Assets	7.72%	8.17%	7.49%	7.64%	
Sales to Fixed Assets	0.66	0.62	0.61	0.67	
Return on Investment	6.21%	5.93%	5.80%	5.81%	
Return on Total Equity	11.55%	10.60%	9.77%	9.95%	
Return on Common Equity	11.55%	10.60%	9.77%	9.95%	
Gross Profit Margin	61.31%	62.73%	63.26%	62.17%	61.46%
INVESTOR ANALYSIS	2018	2017	2016	2015	2014
Degree of Financial Leverage	1.31	1.30	1.39	1.39	1.40
Earnings per Share	0.00	0.00	0.00	0.00	0.00
Price/Earnings Ratio	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Percentage of Earnings Retained	100.00%	100.00%	100.00%	100.00%	100.00%
Dividend Payout	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Dividend Yield					
Book Value per Share	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Materiality of Options					
Oper. Cash Flow per Share					
Oper. Cash Flow/Cash Dividends					
Year-end Market Price					
=====	=====	=====	=====	=====	=====

**BLACK HILLS CORPORATION**  
**CONSOLIDATED STATEMENTS OF INCOME**

Year ended	December 31, 2018	December 31, 2017	December 31, 2016
	(in thousands, except per share amounts)		
Revenue	\$ 1,754,268	\$ 1,680,266	\$ 1,538,916
Operating expenses:			
Fuel, purchased power and cost of natural gas sold	625,610	563,288	499,132
Operations and maintenance	481,706	454,605	426,603
Depreciation, depletion and amortization	196,328	188,246	175,533
Taxes - property and production	51,746	51,578	46,160
Other operating expenses	1,841	5,813	55,307
Total operating expenses	<u>1,357,231</u>	<u>1,263,530</u>	<u>1,202,735</u>
Operating income	<u>397,037</u>	<u>416,736</u>	<u>336,181</u>
Other income (expense):			
Interest charges -			
Interest expense incurred net of amounts capitalized (including amortization of debt issuance costs, premiums and discounts)	(143,720)	(140,533)	(139,091)
Allowance for funds used during construction - borrowed	2,104	2,415	2,981
Interest income	1,641	1,016	1,429
Allowance for funds used during construction - equity	619	2,321	3,270
Other income (expense), net	(1,799)	(213)	1,124
Total other income (expense)	<u>(141,155)</u>	<u>(134,994)</u>	<u>(130,287)</u>
Income before income taxes	255,882	281,742	205,894
Income tax benefit (expense)	23,667	(73,367)	(59,101)
Income from continuing operations	279,549	208,375	146,793
Net (loss) from discontinued operations	(6,887)	(17,099)	(64,162)
Net income	272,662	191,276	82,631
Net income attributable to noncontrolling interest	(14,220)	(14,242)	(9,661)
Net income available for common stock	<u>\$ 258,442</u>	<u>\$ 177,034</u>	<u>\$ 72,970</u>
Amounts attributable to common shareholders:			
Net income from continuing operations	\$ 265,329	\$ 194,133	\$ 137,132
Net (loss) from discontinued operations	(6,887)	(17,099)	(64,162)
Net income (loss) available for common stock	<u>\$ 258,442</u>	<u>\$ 177,034</u>	<u>\$ 72,970</u>
Earnings (loss) per share of common stock, Basic -			
Earnings from continuing operations	\$ 4.88	\$ 3.65	\$ 2.64
(Loss) from discontinued operations	(0.13)	(0.32)	(1.23)
Total earnings per share of common stock, Basic	<u>\$ 4.75</u>	<u>\$ 3.33</u>	<u>\$ 1.41</u>
Earnings (loss) per share of common stock, Diluted -			
Earnings from continuing operations	\$ 4.78	\$ 3.52	\$ 2.57
(Loss) from discontinued operations	(0.12)	(0.31)	(1.20)
Total earnings per share of common stock, Diluted	<u>\$ 4.66</u>	<u>\$ 3.21</u>	<u>\$ 1.37</u>
Weighted average common shares outstanding:			
Basic	<u>54,420</u>	<u>53,221</u>	<u>51,922</u>
Diluted	<u>55,486</u>	<u>55,120</u>	<u>53,271</u>

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

**BLACK HILLS CORPORATION**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

Year ended	December 31, 2018	December 31, 2017	December 31, 2016
	(in thousands)		
Net income	\$ 272,662	\$ 191,276	\$ 82,631
Other comprehensive income (loss), net of tax:			
Benefit plan liability adjustments - net gain (loss) (net of tax of \$(660), \$1,030 and \$757, respectively)	2,155	(1,890)	(1,738)
Benefit plan liability adjustments - prior service (costs) (net of tax of \$0, \$0 and \$107, respectively)	—	—	(247)
Reclassification adjustment of benefit plan liability - net gain (loss) (net of tax of \$(586), \$(585) and \$(600), respectively)	1,901	1,072	1,378
Reclassification adjustment of benefit plan liability - prior service cost (net of tax of \$43, \$69 and \$67, respectively)	(135)	(128)	(154)
Derivative instruments designated as cash flow hedges:			
Net unrealized gains (losses) on interest rate swaps (net of tax of \$0, \$0 and \$10,920, respectively)	—	—	(20,302)
Reclassification of net realized (gains) losses on settled/ amortized interest rate swaps (net of tax of \$(599), \$(1,029) and \$(1,365), respectively)	2,252	1,912	2,534
Net unrealized gains (losses) on commodity derivatives (net of tax of \$(228), \$(135) and \$212, respectively)	755	231	(361)
Reclassification of net realized (gains) losses on settled commodity derivatives (net of tax of \$(31), \$154 and \$4,067, respectively)	99	(516)	(6,938)
Other comprehensive income (loss), net of tax	7,027	681	(25,828)
Comprehensive income	279,689	191,957	56,803
Less: comprehensive income attributable to non-controlling interest	(14,220)	(14,242)	(9,661)
Comprehensive income available for common stock	\$ 265,469	\$ 177,715	\$ 47,142

See Note 16 for additional disclosures related to Comprehensive Income.

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

**BLACK HILLS CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

As of  
December 31, 2018    December 31, 2017  
(in thousands)

**ASSETS**

Current assets:

Cash and cash equivalents	\$ 20,776	\$ 15,420
Restricted cash and equivalents	3,369	2,820
Accounts receivable, net	269,153	248,330
Materials, supplies and fuel	117,299	113,283
Derivative assets, current	1,500	304
Income tax receivable, net	12,978	—
Regulatory assets, current	48,776	81,016
Other current assets	29,982	25,367
Current assets held for sale	—	84,242
Total current assets	503,833	570,782

Investments

41,013                      13,090

Property, plant and equipment

Property, plant and equipment	6,000,015	5,567,518
Less accumulated depreciation and depletion	(1,145,136)	(1,026,088)
Total property, plant and equipment, net	4,854,879	4,541,430

Other assets:

Goodwill	1,299,454	1,299,454
Intangible assets, net	14,337	7,559
Regulatory assets, non-current	235,459	216,438
Other assets, non-current	14,352	10,149
Total other assets, non-current	1,563,602	1,533,600

**TOTAL ASSETS**

\$ 6,963,327    \$ 6,658,902

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

FORM 10K

**BLACK HILLS CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(Continued)

As of  
December 31, 2018    December 31, 2017  


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(in thousands, except share amounts)

**LIABILITIES AND EQUITY**

Current liabilities:			
Accounts payable	\$	210,609	\$ 160,887
Accrued liabilities		215,501	219,462
Derivative liabilities, current		947	2,081
Accrued income tax, net		—	1,022
Regulatory liabilities, current		29,810	6,832
Notes payable		185,620	211,300
Current maturities of long-term debt		5,743	5,743
Current liabilities held for sale		—	41,774
Total current liabilities		648,230	649,101
Long-term debt, net of current maturities		2,950,835	3,109,400
Deferred credits and other liabilities:			
Deferred income tax liabilities, net		311,331	336,520
Regulatory liabilities, non-current		510,984	478,294
Benefit plan liabilities		145,147	159,646
Other deferred credits and other liabilities		109,377	105,735
Total deferred credits and other liabilities		1,076,839	1,080,195
Commitments and contingencies (See Notes 6, 7, 8, 9, 14, 18, 19, and 20)			
Equity:			
Stockholders' equity -			
Common stock \$1 par value; 100,000,000 shares authorized; issued: 60,048,567 and 53,579,986, respectively		60,049	53,580
Additional paid-in capital		1,450,569	1,150,285
Retained earnings		700,396	548,617
Treasury stock at cost - 44,253 and 39,064, respectively		(2,510)	(2,306)
Accumulated other comprehensive income (loss)		(26,916)	(41,202)
Total stockholders' equity		2,181,588	1,708,974
Noncontrolling interest		105,835	111,232
Total equity		2,287,423	1,820,206
<b>TOTAL LIABILITIES AND TOTAL EQUITY</b>	<b>\$</b>	<b>6,963,327</b>	<b>\$ 6,658,902</b>

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

**BLACK HILLS CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

Year ended	December 31, 2018	December 31, 2017	December 31, 2016
	(in thousands)		
<b>Operating activities:</b>			
Net income	\$ 272,662	\$ 191,276	\$ 82,631
Loss from discontinued operations, net of tax	6,887	17,099	64,162
Income (loss) from continuing operations	279,549	208,375	146,793
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, depletion and amortization	196,328	188,246	175,533
Deferred financing cost amortization	7,845	8,261	6,180
Stock compensation	12,390	7,626	10,885
Deferred income taxes	(24,239)	80,992	82,704
Employee benefit plans	14,068	10,141	14,291
Other adjustments, net	5,836	(4,773)	(5,519)
Change in certain operating assets and liabilities:			
Materials, supplies and fuel	(2,919)	(10,089)	1,211
Accounts receivable and other current assets	(45,966)	4,534	(27,172)
Accounts payable and other current liabilities	5,305	(28,222)	(33,023)
Regulatory assets	33,608	(15,407)	3,614
Regulatory liabilities	18,533	(4,536)	(14,082)
Contributions to defined benefit pension plans	(12,700)	(27,700)	(14,200)
Interest rate swap settlement	—	—	(28,820)
Other operating activities, net	6,689	(8,418)	(660)
Net cash provided by operating activities of continuing operations	494,327	409,030	317,735
Net cash provided by (used in) operating activities of discontinued operations	(5,516)	19,231	2,744
Net cash provided by operating activities	488,811	428,261	320,479
<b>Investing activities:</b>			
Property, plant and equipment additions	(457,524)	(326,010)	(454,952)
Acquisition of net assets, net of long-term debt assumed	—	—	(1,124,238)
Purchase of investment	(24,429)	—	—
Other investing activities	(4,281)	1,011	(562)
Net cash (used in) investing activities of continuing operations	(486,234)	(324,999)	(1,579,752)
Net cash provided by (used in) investing activities of discontinued operations	20,385	7,881	(8,413)
Net cash (used in) investing activities	(465,849)	(317,118)	(1,588,165)
<b>Financing activities:</b>			
Dividends paid on common stock	(106,591)	(96,744)	(87,570)
Common stock issued	300,834	4,408	121,619
Net increase (decrease) in commercial paper and short-term borrowings	(25,680)	114,700	19,800
Long-term debt - issuance	700,000	—	1,767,608
Long-term debt - repayments	(854,743)	(105,743)	(1,164,308)
Sale of noncontrolling interest	—	—	216,370
Distributions to noncontrolling interests	(19,617)	(18,397)	(9,561)
Other financing activities	(11,260)	(6,919)	(22,960)
Net cash provided by (used in) financing activities	(17,057)	(108,695)	840,998
Net change in cash, restricted cash and cash equivalents	5,905	2,448	(426,688)
Cash, restricted cash and cash equivalents beginning of year	18,240	15,792	442,480
Cash, restricted cash and cash equivalents end of year	\$ 24,145	\$ 18,240	\$ 15,792

See Note 17 for supplemental disclosure of cash flow information.

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

FORM 10K

**BLACK HILLS CORPORATION**  
**CONSOLIDATED STATEMENTS OF EQUITY**

(in thousands except share amounts)	Common Stock		Treasury Stock		Additional Paid in Capital	Retained Earnings	AOCI	Non controlling Interest	Total
	Shares	Value	Shares	Value					
<b>Balance at December 31, 2015</b>	51,231,861	\$ 51,232	39,720	\$ (1,888)	\$ 953,044	\$ 472,534	\$ (9,055)	\$ —	\$ 1,465,867
Net income (loss) available for common stock	—	—	—	—	—	72,970	—	9,661	82,631
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	(25,828)	—	(25,828)
Dividends on common stock	—	—	—	—	—	(87,570)	—	—	(87,570)
Share-based compensation	145,634	146	(16,165)	668	4,665	—	—	—	5,479
Issuance of common stock	1,968,738	1,969	—	—	118,021	—	—	—	119,990
Issuance costs	—	—	—	—	(1,566)	—	—	—	(1,566)
Dividend reinvestment and stock purchase plan	51,234	50	—	—	2,933	—	—	—	2,983
Other stock transactions	—	—	(8,297)	429	47	—	—	—	476
Sale of noncontrolling interest	—	—	—	—	61,838	—	—	115,395	177,233
Distributions to noncontrolling interest	—	—	—	—	—	—	—	(9,561)	(9,561)
<b>Balance at December 31, 2016</b>	53,397,467	\$ 53,397	15,258	\$ (791)	\$1,138,982	\$ 457,934	\$ (34,883)	\$ 115,495	\$ 1,730,134
Net income (loss) available for common stock	—	—	—	—	—	177,034	—	14,242	191,276
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	681	—	681
Reclassification of certain tax effects from AOCI	—	—	—	—	—	7,000	(7,000)	—	—
Dividends on common stock	—	—	—	—	—	(96,744)	—	—	(96,744)
Share-based compensation	134,266	134	23,806	(1,515)	8,948	—	—	—	7,567
Tax effect of share-based compensation	—	—	—	—	533	3,184	—	—	3,717
Issuance costs	—	—	—	—	(189)	—	—	—	(189)
Dividend reinvestment and stock purchase plan	48,253	49	—	—	3,107	—	—	—	3,156
Redemption of and distributions to noncontrolling interest	—	—	—	—	(1,096)	209	—	(18,505)	(19,392)
<b>Balance at December 31, 2017</b>	53,579,986	\$ 53,580	39,064	\$ (2,306)	\$1,150,285	\$ 548,617	\$ (41,202)	\$ 111,232	\$ 1,820,206
Net income (loss) available for common stock	—	—	—	—	—	258,442	—	14,220	272,662
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	7,027	—	7,027
Reclassification of certain tax effects from AOCI	—	—	—	—	—	—	740	—	740
Reclassification to regulatory asset	—	—	—	—	—	—	6,519	—	6,519
Dividends on common stock	—	—	—	—	—	(106,591)	—	—	(106,591)
Share-based compensation	92,830	93	5,189	(204)	7,301	—	—	—	7,190
Issuance of common stock	6,371,690	6,372	—	—	292,628	—	—	—	299,000
Issuance costs	—	—	—	—	(15)	—	—	—	(15)
Dividend reinvestment and stock purchase plan	4,061	4	—	—	216	—	—	—	220
Other stock transactions	—	—	—	—	154	(72)	—	—	82
Distributions to noncontrolling interest	—	—	—	—	—	—	—	(19,617)	(19,617)
<b>Balance at December 31, 2018</b>	60,048,567	\$ 60,049	44,253	\$ (2,510)	\$1,450,569	\$ 700,396	\$ (26,916)	\$ 105,835	\$ 2,287,423

Dividends per share paid were \$1.93, \$1.81 and \$1.68 for the years ended December 31, 2018, 2017 and 2016, respectively.

The accompanying Notes to Consolidated Financial Statements are an integral part of these Consolidated Financial Statements.

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5)

Balance Sheet (1-5)

**Vertical Analysis**

**BENCHMARK**

**Courtney**

**2018**

5

5

INCOME STATEMENT	2018	2017	2016	2015	2014
Net Sales	100.00%	100.00%	100.00%	100.00%	100.00%
Less: Cost of Goods Sold	35.66%	33.52%	32.43%	35.02%	41.75%
Gross Profit	64.34%	66.48%	67.57%	64.98%	58.25%
Other Operating Revenue	0.00%	0.00%	0.00%	0.00%	0.00%
Less: Operating Expenses	41.71%	41.67%	45.72%	62.70%	39.32%
Operating Income	22.63%	24.80%	21.85%	2.28%	18.93%
Less: Interest Expense (no capitalized interest)	8.19%	8.36%	9.04%	6.61%	5.24%
Other Income (Expenses)	0.15%	0.33%	0.57%	0.53%	0.48%
Unusual or Infreq. Item; Gain (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
Equity in Earnings of Assoc. ; Profit (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
Income before Taxes	14.59%	16.77%	13.38%	-3.80%	14.17%
Less:Taxes Related to Operations	-1.35%	4.37%	3.84%	-1.70%	4.78%
N.I. before Min. Ern.	15.94%	12.40%	9.54%	-2.10%	9.39%
Minority Share of Earnings (Loss)	-0.81%	-0.85%	-0.63%	0.00%	0.00%
N.I. before Nonrecurring Items	15.12%	11.55%	8.91%	-2.10%	9.39%



Oper. of Discontinued Segment;					
Income (Loss)	-0.39%	-1.02%	-4.17%	0.00%	0.00%
Disposal of Discont. Segment;					
Gain (Loss)	0.00%	0.00%	0.00%	-0.36%	0.00%
Extraordinary Item;					
Gain (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
Cum. Effect of Acct Change;					
Gain (Loss)	0.00%	0.00%	0.00%	0.00%	0.00%
	-----	-----	-----	-----	-----
Net Income (Loss)	14.73%	10.54%	4.74%	-2.46%	9.39%
=====	=====	=====	=====	=====	=====

BALANCE SHEET	2018	2017	2016	2015	2014
<b>ASSETS</b>					
Current Assets:					
Cash	0.30%	0.23%	0.21%	9.53%	0.50%
Marketable Securities	0.00%	0.00%	0.00%	0.00%	0.00%
Gross Receivables	3.87%	3.73%	4.04%	3.19%	4.47%
Less: Allowance for Bad Debts	0.00%	0.00%	0.00%	0.00%	0.00%
Net Trade Receivables	3.87%	3.73%	4.04%	3.19%	4.47%
Inventories	1.68%	1.70%	1.65%	1.88%	2.15%
Prepaid Expenses	0.00%	0.00%	0.00%	0.00%	0.00%
Other Current Assets	1.39%	2.91%	1.27%	2.84%	3.57%
<b>Total Current Assets</b>	<b>7.24%</b>	<b>8.57%</b>	<b>7.16%</b>	<b>17.43%</b>	<b>10.69%</b>
Long-Term Assets:					
Net Tangible (Fixed) Assets (other than construction in progress)	69.72%	68.20%	68.59%	70.44%	75.50%
Construction in Progress	0.00%	0.00%	0.00%	0.00%	0.00%
Intangible Assets	0.21%	0.11%	0.13%	0.07%	0.07%
Investments	0.59%	0.20%	0.19%	0.26%	0.41%
Other Nonoperating Assets	22.25%	22.92%	23.92%	11.79%	13.33%
Other Operating Assets	0.00%	0.00%	0.00%	0.00%	0.00%
<b>Total Long-Term Assets</b>	<b>92.76%</b>	<b>91.43%</b>	<b>92.84%</b>	<b>82.57%</b>	<b>89.31%</b>
<b>Total Assets</b>	<b>100.00%</b>	<b>100.00%</b>	<b>100.00%</b>	<b>100.00%</b>	<b>100.00%</b>
<b>LIABILITIES AND EQUITY</b>					
Current Liabilities:					
Accounts Payable	3.02%	2.42%	2.36%	1.94%	2.92%
Short Term Loans	2.67%	3.17%	1.48%	1.66%	1.77%
Current Maturity of L.t. Debt	0.08%	0.09%	0.09%	0.00%	6.48%
Other Current Liabilities	3.54%	4.07%	4.18%	5.18%	4.17%
<b>Total Current Liabilities</b>	<b>9.31%</b>	<b>9.75%</b>	<b>8.10%</b>	<b>8.78%</b>	<b>15.34%</b>
Long-Term Liabilities:					
Long-term Debt	42.38%	46.70%	49.29%	40.07%	29.85%
Reserves	0.00%	0.00%	0.00%	0.00%	0.00%
Deferred Liabilities	4.47%	5.05%	8.22%	9.74%	12.06%
Minority Interest	0.00%	0.00%	0.00%	0.00%	0.00%
Redeemable Preferred	0.00%	0.00%	0.00%	0.00%	0.00%

Other Long-term Liabilities	10.99%	11.17%	7.77%	9.73%	10.86%
	-----	-----	-----	-----	-----
Total Long-term Liabilities	57.84%	62.92%	65.28%	59.53%	52.77%
Total Liabilities	67.15%	72.67%	73.38%	68.32%	68.11%
Shareholders' Equity:					
Preferred Equity	0.00%	0.00%	0.00%	0.00%	0.00%
Common Equity-incl. Ret. Ern.	32.85%	27.33%	26.62%	31.68%	31.89%
	-----	-----	-----	-----	-----
Total Equity	32.85%	27.33%	26.62%	31.68%	31.89%
Total Liabilities and Equity	100.00%	100.00%	100.00%	100.00%	100.00%
=====	=====	=====	=====	=====	=====

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5)

5

Balance Sheet (1-5)

5

**Horizontal Analysis**

**BENCHMARK**

**Courtney**

**2018**

INCOME STATEMENT	2018	2017	2016	2015	2014
Net Sales	125.88%	120.57%	110.43%	93.62%	100.00%
Less: Cost of Goods Sold	107.53%	96.82%	85.79%	78.53%	100.00%
Gross Profit	139.03%	137.59%	128.09%	104.43%	100.00%
Other Operating Revenue	#N/A	#N/A	#N/A	#N/A	#N/A
Less: Operating Expenses	133.53%	127.80%	128.41%	149.28%	100.00%
Operating Income	150.47%	157.93%	127.40%	11.29%	100.00%
Less: Interest Expense (no capitalized interest)	196.83%	192.47%	190.49%	118.16%	100.00%
Other Income (Expenses)	38.49%	83.12%	132.11%	104.46%	100.00%
Unusual or Infreq. Item; Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Equity in Earnings of Assoc. ; Profit (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Income before Taxes	129.55%	142.64%	104.24%	-25.07%	100.00%
Less: Taxes Related to Operations	-35.52%	110.12%	88.71%	-33.26%	100.00%
N.I. before Min. Ern.	213.58%	159.20%	112.15%	-20.90%	100.00%
Minority Share of Earnings (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A

N.I. before Nonrecurring Items	202.71%	148.32%	104.77%	-20.90%	100.00%
Oper. of Discontinued Segment; Income (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Disposal of Discont. Segment; Gain (Loss)	0.00%	0.00%	0.00%	474900.00%	100.00%
Extraordinary Item; Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Cum. Effect of Acct Change; Gain (Loss)	#N/A	#N/A	#N/A	#N/A	#N/A
Net Income (Loss)	197.45%	135.26%	55.75%	-24.53%	100.00%

BALANCE SHEET	2018	2017	2016	2015	2014
<hr/>					
ASSETS					
Current Assets:					
Cash	97.92%	72.67%	64.00%	2077.77%	100.00%
Marketable Securities	#N/A	#N/A	#N/A	#N/A	#N/A
Gross Receivables	141.67%	130.71%	138.58%	77.63%	100.00%
Less: Allowance for Bad Debts	#N/A	#N/A	#N/A	#N/A	#N/A
Net Trade Receivables	141.67%	130.71%	138.58%	77.63%	100.00%
Inventories	128.63%	124.23%	117.57%	95.34%	100.00%
Prepaid Expenses	#N/A	#N/A	#N/A	#N/A	#N/A
Other Current Assets	63.71%	127.77%	54.56%	86.51%	100.00%
<hr/>					
Total Current Assets	110.97%	125.71%	102.81%	177.62%	100.00%
Long-Term Assets:					
Net Tangible (Fixed) Assets (other than construction in progress)					
Construction in Progress	151.46%	141.68%	139.42%	101.67%	100.00%
Intangible Assets	#N/A	#N/A	#N/A	#N/A	#N/A
Investments	451.42%	238.00%	264.23%	106.42%	100.00%
Other Nonoperating Assets	237.15%	75.69%	72.63%	69.30%	100.00%
Other Operating Assets	273.76%	269.65%	275.42%	96.43%	100.00%
<hr/>					
Total Long-Term Assets	#N/A	#N/A	#N/A	#N/A	#N/A
Total Assets	170.35%	160.56%	159.52%	100.75%	100.00%
LIABILITIES AND EQUITY					
Current Liabilities:					
Accounts Payable	164.00%	156.83%	153.45%	108.97%	100.00%
Short Term Loans	169.66%	129.60%	123.63%	72.33%	100.00%
Current Maturity of L.t. Debt	247.49%	281.73%	128.80%	102.40%	100.00%
Other Current Liabilities	2.09%	2.09%	2.09%	0.00%	100.00%
<hr/>					
Total Current Liabilities	139.02%	153.08%	153.61%	135.35%	100.00%
Long-Term Liabilities:					
Long-term Debt	99.53%	99.67%	81.06%	62.39%	100.00%
Reserves	232.79%	245.30%	253.33%	146.24%	100.00%
	#N/A	#N/A	#N/A	#N/A	#N/A

Deferred Liabilities	60.81%	65.73%	104.62%	88.01%	100.00%
Minority Interest	#N/A	#N/A	#N/A	#N/A	#N/A
Redeemable Preferred	#N/A	#N/A	#N/A	#N/A	#N/A
Other Long-term Liabilities	165.98%	161.25%	109.78%	97.61%	100.00%
-----					
Total Long-term Liabilities	179.75%	186.97%	189.81%	122.92%	100.00%
Total Liabilities	161.68%	167.31%	165.32%	109.29%	100.00%
Shareholders' Equity:					
Preferred Equity	#N/A	#N/A	#N/A	#N/A	#N/A
Common Equity-incl. Ret. Ern.	168.95%	134.44%	128.11%	108.27%	100.00%
-----					
Total Equity	168.95%	134.44%	128.11%	108.27%	100.00%
Total Liabilities and Equity	164.00%	156.83%	153.45%	108.97%	100.00%
=====					

FinSAS Version 2003051213

Company:

Analyst:

Most Recent Year Available:

Years Available for:

Income Statement (1-5)

Balance Sheet (1-5)

**Ratios - average**

**BENCHMARK**

**Courtney**

**2018**

5

5

LIQUIDITY	2018	2017	2016	2015	2014
Days' Sales in Receivables	56.00	53.94	62.45	41.26	49.76
Accounts Receivable Turnover	6.78	6.57	7.49	7.73	
A/R Turnover in Days	53.83	55.57	48.71	47.21	
Days' Sales in Inventory	68.44	73.41	78.40	69.46	57.21
Inventory Turnover	5.43	5.11	5.14	5.13	
Inventory Turnover in Days	67.26	71.44	70.99	71.15	
Operating Cycle	121.10	127.01	119.70	118.36	
Working Capital	(144,397)	(78,319)	(61,118)	400,122	(197,245)
Current Ratio	0.78	0.88	0.88	1.98	0.70
Acid Test	0.45	0.41	0.52	1.45	0.32
Cash Ratio	0.03	0.02	0.03	1.08	0.03
Sales to Working Capital	-15.75	-24.10	9.08	12.86	
Cash Flow/Cur. Mat. of Debt & NP	0.00	0.00	0.00	0.00	0.00
LONG-TERM DEBT-PAYING ABILITY	2018	2017	2016	2015	2014
Times Interest Earned	2.78	3.00	2.48	0.43	3.71
Fixed Charge Coverage	2.78	3.00	2.48	0.43	3.71
Debt Ratio	67.15%	72.67%	73.38%	68.32%	68.11%
Debt/Equity	204.42%	265.83%	275.65%	215.63%	213.61%
Debt to Tangible Net Worth	205.71%	266.94%	276.99%	216.12%	214.11%
Cash Flow/Total Debt	0.00%	0.00%	0.00%	0.00%	0.00%



PROFITABILITY	2018	2017	2016	2015	2014
Net Profit Margin	15.94%	12.40%	9.54%	#N/A	9.39%
Total Asset Turnover	0.26	0.26	0.28	0.29	
Return on Assets	4.10%	3.16%	2.63%	#N/A	
Operating Income Margin	22.63%	24.80%	21.85%	2.28%	18.93%
Operating Asset Turnover	0.34	0.33	0.34	0.34	
Return on Operating Assets	7.58%	8.29%	7.47%	0.77%	
Sales to Fixed Assets	0.37	0.37	0.40	0.40	
Return on Investment	6.87%	5.82%	5.60%	1.51%	
Return on Total Equity	12.92%	10.92%	8.57%	#N/A	
Return on Common Equity	12.92%	10.92%	8.57%	#N/A	
Gross Profit Margin	64.34%	66.48%	67.57%	64.98%	58.25%
INVESTOR ANALYSIS	2018	2017	2016	2015	2014
Degree of Financial Leverage	1.56	1.50	1.68	#N/A	1.37
Earnings per Share	0.00	0.00	0.00	0.00	0.00
Price/Earnings Ratio	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Percentage of Earnings Retained	100.00%	100.00%	100.00%	#N/A	100.00%
Dividend Payout	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Dividend Yield					
Book Value per Share	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!
Materiality of Options					
Oper. Cash Flow per Share					
Oper. Cash Flow/Cash Dividends					
Year-end Market Price					
=====	=====	=====	=====	=====	=====

## **APPENDIX B**

# Projections and Valuation

Estimated price for most recent fiscal year	12/31/18	=	\$	33.41
Estimated price for target date	12/31/23	=	\$	11.50

	Most Recent 12/31/18	Projected 12/31/19	Projected 12/31/20	Projected 12/31/21	Projected 12/31/22	Projected 12/31/23	Projected 12/31/24
<b>Income Statement (\$ Thousands)</b>							
Sales	\$ 916,447	\$ 1,008,092	\$ 1,098,277	\$ 1,186,059	\$ 1,270,623	\$ 1,351,297	\$ 1,427,548
Costs of goods sold (COGS)	696,807	766,488	825,138	880,374	931,665	978,611	1,020,936
Sales, general and administrative expense (SGA)	21,094	23,203	28,087	33,076	38,094	43,072	47,949
Depreciation	74,666	82,129	84,828	87,065	88,869	90,274	91,318
Operating profit	\$ 123,880	\$ 136,271	\$ 160,225	\$ 185,544	\$ 211,995	\$ 239,340	\$ 267,345
Interest expense	26,947	31,720	31,605	37,838	49,563	58,573	67,937
Interest income	0	0	0	0	0	0	0
Nonoperating income (Expense)	(10,977)	(12,075)	(13,155)	(14,207)	(15,220)	(16,186)	(17,099)
Earnings before taxes (EBT)	\$ 85,956	\$ 92,476	\$ 115,464	\$ 133,499	\$ 147,213	\$ 164,581	\$ 182,309
Tax expense	3,611	23,119	28,866	33,375	36,803	41,145	45,577
Net income before extraordinary items	\$ 82,345	\$ 69,357	\$ 86,598	\$ 100,124	\$ 110,409	\$ 123,436	\$ 136,732
After-tax extraordinary income (Expense)	0	0	0	0	0	0	0
<b>Net income (NI)</b>	<b>\$ 82,345</b>	<b>\$ 69,357</b>	<b>\$ 86,598</b>	<b>\$ 100,124</b>	<b>\$ 110,409</b>	<b>\$ 123,436</b>	<b>\$ 136,732</b>
Dividends-- preferred	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Dividends-- common	\$ 53,198	\$ 65,966	\$ 81,785	\$ 101,379	\$ 125,632	\$ 155,632	\$ 192,701
Additions to RE	\$ 29,147	\$ 3,392	\$ 4,813	\$ (1,254)	\$ (15,223)	\$ (32,196)	\$ (55,969)

## Balance Sheets (\$ Thousands)

	12/31/18	12/31/19	12/31/20	12/31/21	12/31/22	12/31/23	12/31/24
<b>Assets</b>							
Cash	\$ 861	\$ 10,081	\$ 10,156	\$ 10,160	\$ 10,101	\$ 9,989	\$ 9,833
Inventory	106,270	116,897	131,330	145,711	159,865	173,638	186,900
Accounts receivable	75,144	82,658	90,053	97,251	104,185	110,800	117,052
Other short-term operating assets	59,145	65,060	70,880	76,545	82,003	87,209	92,130
Short-term investments	0	0	0	0	0	0	0
<b>Total current assets</b>	<b>\$ 241,420</b>	<b>\$ 274,696</b>	<b>\$ 302,419</b>	<b>\$ 329,667</b>	<b>\$ 356,153</b>	<b>\$ 381,636</b>	<b>\$ 405,914</b>
Net plant, property, & equipment (PPE)	1,399,472	1,539,356	1,589,935	1,631,869	1,665,685	1,692,021	1,711,579
Other long-term operating assets	402,664	442,930	482,556	521,125	558,280	593,726	627,229

Long-term investments	8,961	9,857	10,739	11,597	12,424	13,213	13,959
<b>Total Assets</b>	<b>\$ 2,052,517</b>	<b>\$ 2,266,839</b>	<b>\$ 2,385,649</b>	<b>\$ 2,494,258</b>	<b>\$ 2,592,543</b>	<b>\$ 2,680,596</b>	<b>\$ 2,758,680</b>
<b>Liabilities and Equity</b>							
Accounts payable (AP)	\$ 96,291	\$ 105,920	\$ 115,396	\$ 124,619	\$ 133,504	\$ 141,981	\$ 149,992
Accruals	0	0	0	0	0	0	0
Other operating current liabilities	73,630	80,993	88,239	95,291	102,086	108,567	114,693
All short-term debt	172	674,055	461,548	239,007	20,314	(185,910)	(367,693)
<b>Total current liabilities</b>	<b>\$ 170,093</b>	<b>\$ 860,969</b>	<b>\$ 665,182</b>	<b>\$ 458,917</b>	<b>\$ 255,904</b>	<b>\$ 64,638</b>	<b>\$ (103,007)</b>
Long-term debt	590,002	53,701	310,495	575,254	842,476	1,107,126	1,364,681
Deferred taxes	0	0	0	0	0	0	0
Preferred stock	0	0	0	0	0	0	0
Other long-term liabilities	563,559	619,915	672,904	724,273	773,573	820,437	864,580
<b>Total liabilities</b>	<b>\$ 1,323,654</b>	<b>\$ 1,534,585</b>	<b>\$ 1,648,581</b>	<b>\$ 1,758,444</b>	<b>\$ 1,871,952</b>	<b>\$ 1,992,201</b>	<b>\$ 2,126,255</b>
Par plus PIC Less treasury (and other adjustments)	637,248	637,248	637,248	637,248	637,248	637,248	637,248
Retained earnings (RE)	91,615	95,007	99,820	98,566	83,343	51,147	(4,822)
<b>Total common equity</b>	<b>\$ 728,863</b>	<b>\$ 732,255</b>	<b>\$ 737,068</b>	<b>\$ 735,814</b>	<b>\$ 720,591</b>	<b>\$ 688,395</b>	<b>\$ 632,426</b>
<b>Total liabilities and equity</b>	<b>\$ 2,052,517</b>	<b>\$ 2,266,839</b>	<b>\$ 2,385,649</b>	<b>\$ 2,494,258</b>	<b>\$ 2,592,543</b>	<b>\$ 2,680,596</b>	<b>\$ 2,758,680</b>

### Info for making the sheets balance

Specified assets	2,266,839	2,385,649	2,494,258	2,592,543	2,680,596	2,758,680
Specified liabilities	1,593,478	998,189	1,267,307	1,526,598	1,768,039	1,980,368
Net required financing	673,362	1,387,460	1,226,951	1,065,945	912,557	778,312
Current debt	673,362	1,387,460	1,226,951	1,065,945	912,557	778,312
Short-term investments	0	0	0	0	0	0
<b>Balance check: TA-TL</b>	<b>Balance</b>	<b>Balance</b>	<b>Balance</b>	<b>Balance</b>	<b>Balance</b>	<b>Balance</b>

### Valuation

#### Calculating Projected FCF

Marginal tax rate	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Reported income tax expense	3,611	23,119	28,866	33,375	36,803	41,145
Taxes reported but not paid	0	0	0	0	0	0

Actual taxes paid	3,611	23,119	28,866	33,375	36,803	41,145	45,577
Plus tax saved due to net interest expenses	6,737	7,930	7,901	9,460	12,391	14,643	16,984
Minus tax paid on non-operating income	<u>(2,744)</u>	<u>(3,019)</u>	<u>(3,289)</u>	<u>(3,552)</u>	<u>(3,805)</u>	<u>(4,047)</u>	<u>(4,275)</u>
Tax on operating income	13,092	34,068	40,056	46,386	52,999	59,835	66,836
Net operating profit after taxes (NOPAT)	110,788	102,204	120,169	139,158	158,996	179,505	200,509
NOPAT adjusted for extraordinary income	110,788	102,204	120,169	139,158	158,996	179,505	200,509
Operating current assets	241,420	274,696	302,419	329,667	356,153	381,636	405,914
Operating current liabilities	169,921	186,913	203,635	219,911	235,590	250,548	264,686
Net operating working capital	71,499	87,783	98,784	109,756	120,564	131,088	141,228
Operating long term capital	1,802,136	1,982,286	2,072,491	2,152,994	2,223,965	2,285,747	2,338,808
Operating capital (adjusted for any special asset impairment of accou	1,873,635	2,070,069	2,171,275	2,262,750	2,344,529	2,416,835	2,480,036
Investment in operating capital	134,453	196,434	101,206	91,475	81,779	72,306	63,201
Free cash flow (including extraordinary income)	(23,665)	(94,231)	18,962	47,683	77,218	107,199	137,308

### Calculating Projected ROIC

ROIC (NOPAT/ Beginning capital)	6.4%	5.5%	5.8%	6.4%	7.0%	7.7%	8.3%
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### Projected Growth Rates

Growth in Sales		10.0%	8.9%	8.0%	7.1%	6.3%	5.6%
Growth in NOPAT		-7.7%	17.6%	15.8%	14.3%	12.9%	11.7%
Growth in operating capital		10.5%	4.9%	4.2%	3.6%	3.1%	2.6%
Growth in FCF		298.2%	-120.1%	151.5%	61.9%	38.8%	28.1%

### Calculating Value

WACC	8.36%	8.36%	8.36%	8.36%	8.36%	8.36%	8.36%
Assumed long-term return on invested capital							
Horizon value							
Value of operations	2,372,744	2,665,368	2,869,267	3,061,494	3,240,259	3,403,990	3,551,302
Value of operations adjusted for half-year convention	2,469,950	2,774,562	2,986,814	3,186,916	3,373,005	3,543,443	3,696,790
Value of investments	8,961	9,857	10,739	11,597	12,424	13,213	13,959
Total value of firm	2,478,911	2,784,419	2,997,553	3,198,513	3,385,429	3,556,656	3,710,749
Value of all debt, preferred stock, and other nonoperating liabilities	1,153,733	1,347,671	1,444,947	1,538,534	1,636,362	1,741,653	1,861,569
Value of equity	1,325,178	1,436,748	1,552,607	1,659,979	1,749,066	1,815,003	1,849,180
Number of shares	39,665	39,665	39,665	39,665	39,665	39,665	39,665
<b>Estimated price per share, end of fiscal year</b>	<b>\$ 33.41</b>	<b>\$ 36.22</b>	<b>\$ 39.14</b>	<b>\$ 41.85</b>	<b>\$ 44.10</b>	<b>\$ 45.76</b>	<b>\$ 46.62</b>

## **Price per share on target date**

Most recent actual fiscal year end	12/31/18	
Target valuation date	12/31/23	
Most recent fiscal year-end prior to target date	12/31/18	
Number of days from target to fiscal year-end prior to target	1826.00	
Value of operations on target date	4,419,348	
Value of investments on target date	13,444	13,444
Total value of firm on target date	4,432,792	
Value of debt, preferred stock, and other nonoperating liabilities on target date	2,123,957	2,179,881
Value of equity on target date	2,308,835	
Number of shares on target date	200,788	
<b>Price per share, target date</b>	<b>\$ 11.50</b>	

## **Selected Projected Ratios and Other Data**

Projected economic profit (EP)	110,788	(54,458)	(52,917)	(42,390)	(30,200)	(16,530)	(1,571)
Projected market value added (MVA)	596,315	704,493	815,539	924,166	1,028,475	1,126,608	1,216,754
Price/earnings ratio (P/E ratio)	16.1	20.7	17.9	16.6	15.8	14.7	13.5
Market to book ratio	1.8	2.0	2.1	2.3	2.4	2.6	2.9
Value/EBITDA ratio	12.5	12.7	12.2	11.7	11.3	10.8	10.3
Value/Sales ratio	2.7	2.8	2.7	2.7	2.7	2.6	2.6
Times-interest-earned ratio	4.6	4.3	5.1	4.9	4.3	4.1	3.9
Long-term debt/value of operations		1.9%	10.4%	18.1%	25.0%	31.2%	36.9%

## **Statement of Cash Flows**

### **Operating Activities**

Net income	\$ 82,345	\$ 69,357	\$ 86,598	\$ 100,124	\$ 110,409	\$ 123,436	\$ 136,732
Depreciation	74,666	82,129	84,828	87,065	88,869	90,274	91,318
Change in deferred tax	0	0	0	0	0	0	0
Change in inventory	(18,236)	(10,627)	(14,433)	(14,381)	(14,154)	(13,773)	(13,261)
Change in accounts receivable	(6,678)	(7,514)	(7,395)	(7,198)	(6,934)	(6,615)	(6,252)
Change in other short-term operating assets	7,266	(5,915)	(5,820)	(5,665)	(5,458)	(5,206)	(4,921)
Change in accounts payable	11,614	9,629	9,476	9,223	8,885	8,476	8,012
Change in accruals	0	0	0	0	0	0	0

Change in other current liabilities	<u>(98,160)</u>	<u>7,363</u>	<u>7,246</u>	<u>7,053</u>	<u>6,794</u>	<u>6,482</u>	<u>6,126</u>
<b>Net cash from operating activities</b>	\$ 52,817	\$ 144,423	\$ 160,500	\$ 176,222	\$ 188,413	\$ 203,074	\$ 217,753
<b>Investing Activities</b>							
Investment in PPE	\$ (75,602)	\$ (222,013)	\$ (135,407)	\$ (128,999)	\$ (122,685)	\$ (116,610)	\$ (110,876)
Investment in other long-term oper. ass.	<u>(44,678)</u>	<u>(40,266)</u>	<u>(39,625)</u>	<u>(38,569)</u>	<u>(37,155)</u>	<u>(35,446)</u>	<u>(33,503)</u>
<b>Net cash from investing activities</b>	\$ (120,280)	\$ (262,280)	\$ (175,033)	\$ (167,568)	\$ (159,840)	\$ (152,056)	\$ (144,379)
<b>Financing Activities</b>							
Change in short-term investments	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Change in long-term investments	(332)	(896)	(882)	(858)	(827)	(789)	(746)
Change in short-term debt	(14)	673,883	(212,508)	(222,541)	(218,693)	(206,224)	(181,783)
Change in long-term debt	99,622	(536,301)	256,794	264,759	267,221	264,651	257,555
Preferred dividends	0	0	0	0	0	0	0
Change in preferred stock	0	0	0	0	0	0	0
Change in other long-term liabilities	3,206	56,356	52,989	51,369	49,300	46,864	44,143
Change in common stock (Par + PIC)	2,824	0	0	0	0	0	0
Common dividends	<u>(53,198)</u>	<u>(65,966)</u>	<u>(81,785)</u>	<u>(101,379)</u>	<u>(125,632)</u>	<u>(155,632)</u>	<u>(192,701)</u>
<b>Net cash from financing activities</b>	\$ 52,108	\$ 127,077	\$ 14,608	\$ (8,649)	\$ (28,631)	\$ (51,130)	\$ (73,531)
<b>Net cash flow</b>	\$ (15,355)	\$ 9,220	\$ 75	\$ 4	\$ (59)	\$ (112)	\$ (157)
Starting cash	<u>16,216</u>	<u>861</u>	<u>10,081</u>	<u>10,156</u>	<u>10,160</u>	<u>10,101</u>	<u>9,989</u>
Ending cash	<u>\$ 861</u>	<u>\$ 10,081</u>	<u>\$ 10,156</u>	<u>\$ 10,160</u>	<u>\$ 10,101</u>	<u>\$ 9,989</u>	<u>\$ 9,833</u>

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