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MDU - Q2 2023 MDU Resources Group Inc Earnings Call

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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Hello. My name is Lynette, and I will be your conference facilitator. At this time, I would like to welcome everyone to the MDU Resources Group 2023 Second Quarter Conference Call.

(Operator Instructions)

The webcast can be accessed at www.mdu.com under the Investor Relations heading. Select Events and Presentations and click Q2 2023 Earnings Conference call. After the conclusion of the webcast, a replay will be available at the same location.

I would now like to turn the conference over to Jason Vollmer, Vice President, Chief Financial Officer and Treasurer of MDU Resources Group. Please go ahead, sir.

Jason L. Vollmer - MDU Resources Group, Inc. – VP, CFO & Treasurer

Thank you, Lynette, and welcome, everyone, to our second quarter 2023 earnings conference call. You can find our earnings release and supplemental materials for this call on our website at www.mdu.com, under the Investor Relations tab.

Leading today's discussion along with me, will be Dave Goodin, President and CEO of MDU Resources. Also with us today to answer questions following our prepared remarks are: Stephanie Barth, Vice President, CAO and Controller of MDU Resources; Nicole Kivisto, President and CEO of our Utility Group; Rob Johnson, President of WBI Energy; and Jeff Thiede, President and CEO of MDU Construction Services Group.

During our call, we will make certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. Although the company believes that its expectations and beliefs are based on reasonable assumptions, actual results may differ materially. For more information about the risks and uncertainties that could cause our actual results to vary from any forward-looking statements, please refer to our most recent SEC filings.

We may also refer to certain non-GAAP information. For a reconciliation of any non-GAAP information to the appropriate GAAP metric, please reference our earnings news release. I'll provide consolidated financial results for the second quarter before handing the call over to Dave for his formal comments and forward look.

This morning, we announced second quarter earnings of \$130.7 million or 64 cents per share on a GAAP basis compared to second quarter 2022 GAAP earnings of \$70.7 million, or 35 cents per share. Second quarter income from continuing operations was \$147.6 million, or 72 cents per share.

It's important to note that with the spin-off of Knife River being completed during the quarter, Knife River's results and other related impacts are reported as discontinued operations in our GAAP-based results for the current and prior year. As such, with the completion of the spin-off and work continuing with the tax-advantaged separation of our Construction Services business, we are also reporting adjusted income from continuing operations to provide financial results that more closely correlate to, and better outline the strength of our ongoing business operations.

These adjustments reflect the May 31 spin-off of approximately 90% of the outstanding shares of Knife River Corporation, including the unrealized gain on the retained shares as well as any other items related to our strategic initiatives. For more information on these adjustments, please see the table provided on Page 7 of our earnings news release.

We experienced outstanding results from our businesses in the second quarter, with adjusted income from continuing operations of \$60 million, or 29 cents per share, compared to second quarter 2022 adjusted income from continuing operations of \$36.1 million or 18 cents per share. As we look at the individual businesses, our combined utility business reported earnings of \$13.1 million for the quarter, compared to a loss of \$2.9 million in the second quarter of 2022.

The electric utility reported second quarter earnings of \$16.3 million, compared to \$4.6 million for the same period in 2022. The increase was largely the result of higher retail sales due to interim rate relief in North Dakota and Montana, and a 31.4% increase in commercial and residential volumes.

The volume increase is primarily the result of warmer weather and an electric service agreement to provide power to a data center near Ellendale, North Dakota. Also driving the increase in earnings was lower operation and maintenance expense, largely related to the absence of a prior year planned maintenance outage at one of our generating stations, and lower payroll-related costs. This business also experienced higher investment returns on nonqualified benefit plans.

Our natural gas utility reported a seasonal loss of \$3.2 million in the second quarter, compared to a loss of \$7.5 million in the second quarter of 2022. Revenues increased primarily from higher basic service charges and approved rate relief in Washington and Idaho. The business also benefited from increased investment returns on nonqualified benefit plans during the quarter. Warmer spring weather led to a 12.5% decrease in retail sales volumes to all customer classes during the quarter, which was partially offset by weather normalization and decoupling mechanisms.

Increased operation and maintenance expense, primarily higher payroll-related costs, as well as higher interest expense, added to the seasonal loss, which was partially offset by increased interest income associated with higher purchased gas cost adjustment balances.

The pipeline business earned \$8.7 million in the second quarter, compared to \$7.1 million from this time last year. The improvement in earnings was driven by higher transportation and storage-related revenues. This business experienced record quarterly transportation volumes, largely due to increased contracted volume commitments from the North Bakken Expansion project.

The pipeline business also benefited from non-regulated projects revenue and increased investment returns on nonqualified benefit plans during the quarter. The increase was partially offset by higher operation and maintenance expense, primarily due to higher payroll-related costs and non-regulated project costs. In addition, interest expense increased as a result of higher interest rates and higher debt balances.

Construction services reported record second quarter revenue of \$747 million and record second quarter earnings of \$38.6 million, compared to revenue of \$685.4 million and earnings of \$34.5 million for the same period in 2022. EBITDA increased \$10.6 million in the second quarter, compared to the prior year.

Commercial utility, industrial and institutional workloads, all increased for the quarter, which drove the record second quarter revenue. Gross profit increased, largely due to product mix in the commercial, industrial and institutional markets, offset in part by lower renewable project revenue and

gross profit. This business also saw higher selling, general and administrative costs, largely higher payroll-related costs, and higher interest expense from increased working capital needs and higher interest rates.

As I mentioned, results at each of our businesses were positively impacted in the second quarter on a non-cash basis by higher investment returns on nonqualified benefit plans. Collectively, the positive earnings variance was approximately \$8.4 million, or 4 cents per share, when compared to the second quarter of 2022. This change in investment returns is due to fluctuations in the financial markets. That summarizes the financial highlights for the quarter.

I'll now turn the call over to Dave for his formal remarks. Dave?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Thank you, Jason, and thank you everyone for spending time with us today and for your continued interest in MDU Resources. The second quarter was historic for our company as we completed the separation of Knife River Corporation on May 31st and experienced outstanding performance from all of our remaining businesses during the quarter. The Knife River separation was a monumental achievement for both our company and Knife River, and to add record results across our remaining businesses during the quarter makes me extremely proud of and grateful for our hardworking and dedicated employees.

Our utility and natural gas pipeline businesses continued to perform well. The utility was positively impacted by rate relief and higher electric retail sales volumes during the quarter. The pipeline business had record quarterly transportation volumes as we continue to see the benefit of increased contracted volume commitments, particularly on our North Bakken Expansion project.

Construction Services had record second quarter revenues, earnings, and EBITDA, driven by increased workloads and increased gross profit. While completing this record amount of work, construction services continues to see strong demand and secure additional projects to replace its completed and nearly completed projects, reporting record second quarter backlog.

To summarize activity by business segment, I'll start off with the regulated energy delivery businesses. The utility reported increased earnings on a combined basis for the quarter, driven by rate relief in certain electric and natural gas jurisdictions. Electric retail sales were 31.4% higher, which was due in part to warmer temperatures that increased customer usage, but also due to bringing on a new large-volume customer during the quarter.

We expect Heskett Unit 4 to be operational later this year as we finish construction on the 88-megawatt natural gas-fired electric generating facility located across the river here just in North Mandan. We also continue to expect rate base to grow between 6-7 percent, compounded annually over the next 5 years, driven primarily by investments in system infrastructure, upgrades and replacements to safely meet customer demand.

We have received approvals on settlements in North Dakota electric and Idaho natural gas rate cases, with new rates effective July 1st for both, and we filed an all-party settlement in the Montana electric case. Our utility continues to seek timely regulatory recovery for the investments associated with providing safe and reliable electric and natural gas and electric service to our growing customer base, as we expect to file three general rate cases yet this year and one more in early 2024.

Our pipeline business performed very well during the quarter. As Jason noted, this business recorded higher transportation and storage-related revenues during the quarter and had record quarterly natural gas transportation volumes.

In January of 2023, WBI Energy filed a general rate case with the Federal Energy Regulatory Commission for increases in its transportation and storage service rates. These rates take effect on August 1, subject to refund. In the event of a rate case settlement agreement, of which the Company is in active discussions with the FERC and its customers on, the rates outlined in the settlement agreement would take effect in August of 2023.

We began construction in the second quarter here on three natural gas pipeline expansion projects that are anticipated to be in service later in 2023. These projects will add approximately 300 million cubic feet per day of incremental capacity, increasing the total capacity from 2.4 billion to 2.7 billion cubic feet per day.

With the strong start to the year for our regulated energy delivery business, we are increasing earnings guidance for the regulated businesses to a range of \$150 million to \$160 million, up \$10 million from our previous range of \$140 million to \$150 million.

Now I'd like to move on to our construction services business. As I mentioned previously, demand remains strong for our construction services business, evidenced by our record second quarter revenue, earnings, EBITDA and backlog. We are well positioned to complete these projects safely and efficiently with our ability to attract and retain a skilled workforce of 8,500 employees across our 40-plus state footprint.

We are affirming our 2023 revenue guidance range of \$2.8 billion to \$3 billion and we expect slightly higher margins compared to 2022, and EBITDA in the range of \$200 million to \$225 million.

On July 10, we announced that our Board of Directors determined that we will pursue a potential tax-advantaged separation of our construction services business. After an extensive strategic review, the board determined that this was the best path forward to optimize value for stockholders while achieving our objective of becoming a pure-play regulated company. We are focused on determining the best method and timeline to effect the separation and will keep you updated as we proceed.

Looking forward, our construction services business is well positioned to benefit from increased bidding opportunities. With the funding from the Infrastructure Investment and Jobs Act and the Inflation Reduction Act, our construction services business will see increased demand in 2023 and beyond for the work it already excels in.

Overall, as we look ahead, we are encouraged by our opportunities for ongoing customer and system growth in our electric and natural gas utilities, our robust slate of pipeline expansion projects and steady demand for pipeline services, and high demand for our construction services.

We also announced today that the Board of Directors declared a quarterly dividend on the company's common stock of 12.5 cents per share. This change in dividend reflects our intent to align our payout relative to the regulated energy delivery earnings with pure-play regulated peer companies. The dividend is payable October 1st, to stockholders of record on September 14.

Along with this announcement, we established a new dividend payout ratio target of 60% to 70% of our regulated energy delivery earnings. We are proud of our 85-year history of returning capital to our shareholders through the dividend, and feel this new target payout ratio will allow us to continue this practice, while reinvesting in the growth of our regulated operations as we progress on our strategic path of becoming a pure-play regulated company.

As always, MDU Resources is committed to operating with integrity and with a focus on safety while creating superior shareholder value, as we continue providing essential products and services to our customers and communities, while being a great and safe place to work.

I appreciate your interest in and commitment to MDU Resources and ask now that we open the line for further questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

I'll take your first question from Dariusz Lozny from Bank of America.

Dariusz Lozny - BofA Securities, Research Division - Research Analyst

Maybe just starting off on the CSG transaction. Can you discuss at all the specific methods or perhaps when you might be able to update the market as far as what you're considering and time line for the transaction?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. Certainly, Dariusz, I appreciate you calling in. And certainly, your question is top of mind for here as well. I'll just maybe step back for a moment. Certainly, our main focus here is how do we optimize the value here for our shareholders. I think that is very central to our thinking.

CSG is certainly a great performing business that's evidenced again by the second quarter results that we just posted here. And when we think of the backlog at a record level, even with record levels of revenue, we think it's performing very well. Certainly, as we think about that business, certainly, we've done recently a spin with our Knife River, and that could be in that tax-advantage category as well. But we're also looking at other alternatives here as well.

So for as the time line is concerned, I would say there's been no final determination on the means of the tax-advantage separation, certainly update you and the market as we go along. I just would remind you that we're going to be very diligent here, but I think we've also demonstrated also our ability to do this kind of thing. And with that, I'll just stop there, but we'll certainly update the market along the way.

Dariusz Lozny - BofA Securities, Research Division - Research Analyst

Okay. Certainly appreciate that color. Maybe one on the updated guidance range for the year. Can you unpack or quantify at all the relative contributions to the higher guidance range from -- so obviously got a tailwind from the nonqualified plan. You've got the new large customer that you mentioned at the electric utility. And also it looks like some pretty constructive execution on the regulatory front. Can you maybe it all rank how each of those or perhaps other factors contributed to the guide up?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. No, I appreciate you noting that. Certainly, we're guiding up basically 7%. If you think midpoint to midpoint from prior range to new range, if you just kind of quantify that. I would say the things you noted there are all contributory to that. Certainly, we've had favorable weather in the first part of the year. We saw that with a strong winter volumes, if you will. And then we went quickly from winter to an extended late winter, right into summer, which helped some of the electric volumes there. So we saw that.

The large volume customer certainly is incremental to, as we think about the year, it's large volume, low margin, but at the same time, the additive. And then certainly, the regulatory activity that Nicole and her team have done with the completion, both North Dakota and Idaho and then an all-party settlement for Montana, those all have contributed in addition to Rob ramping up on North Bakken Expansion, which we had expected, frankly, year-over-year.

So we're very pleased with the progress, hence, raising the guidance for the back half. So I think you're spot on to quantify those, they all contributed, I would say.

Dariusz Lozny - BofA Securities, Research Division - Research Analyst

Okay. Great. One more, if I can. I just wanted to ask about the segment-level guidance for CSG specifically. You guys are pointing to interest expense of \$15 million for the full year. And it looks like it's pretty modest for the first half of the year. Are you expecting to issue some debt at that segment in the second half of the year?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes, I'll ask Jason since it's kind of a financing question that you've got. But as a reminder, again, we're holding our guidance from -- we raised guidance on the revenue side at the end of first quarter by \$50 million. We're holding that \$2.8 million to \$3.0 million for the remainder of the year and noting margins to be slightly higher on a year-over-year. But I think your question is more zeroed in on interest expense and what we're thinking there, correct? I just want to make sure we're answering your question.

Dariusz Lozny - BofA Securities, Research Division - Research Analyst

Yes, that's correct. The guidance implies an uptick in the second half of the year. So I was just wondering if there is implicit in that is an issuance of some incremental debt at that segment.

Jason L. Vollmer - MDU Resources Group, Inc. – VP, CFO & Treasurer

Yes. I can jump in there, Dariusz. This is Jason. I think from our perspective, as we look at this, I mean we really are focused on the guidance range that we put out there for the revenue and the EBITDA side of things. That's really where we're putting most of our focus at, obviously, with EBITDA, we reconcile back to an earnings number, which is probably where you're referencing some of those add-backs, I think, throughout that process.

As we look at it as a range of outcomes there, I think, that we could see. We aren't looking specifically at any additional debt issuance there. What we have seen with CSG, as we mentioned, higher financing costs, higher interest expense even here in the first quarter is that working capital numbers have been a little bit higher with this business as we've seen the vast amount of work that they've been working through here and the increase in backlogs along the way. That, along with higher interest rates that we have seen have had an impact there as well.

So really what we're kind of pointing to at this point is the expectation that we would see some of that persist here into the second half of the year. I won't get specific on interest cost itself. We really don't give guidance at that level, but there is some impact, I think, as we look at just kind of the balances that we see here today.

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Say, Dariusz, maybe tied into that, but it's more of a question for you. Would you be interested in hearing from Jeff Thiede more operationally, how he's thinking about the business, particularly the back half of the year?

Dariusz Lozny - BofA Securities, Research Division - Research Analyst

Certainly, that would be very helpful.

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. Jeff, could you weigh in given what you're seeing on the ground there?

Jeffrey S. Thiede - President & CEO of MDU Construction Services Group, Inc

Absolutely. We're continuing to see strong demand for our services as reflected in our record Q2 backlog. And that's also complemented by our record second quarter revenues or second quarter earnings. Our backlog is very broad-based. But on the other hand, it's very diversified.

We're building some of the most innovative and largest projects in multiple geographic regions across the country in the markets that we serve. And several of those projects, of course, in Las Vegas are headliner-type projects that are well underway, and there are more projects ahead on our radar for the future.

You look at our T&D side, and we have a lot of our service agreements, our MSAs that have been negotiated and renewed, reflected our updated labor material, fuel equipment costs, that's going to be a contributing factor to our success going forward. In addition, we've got some exciting projects in our T&D sector. We're underway in Kansas City on a street car extension project in U.S. 69 Express Lane. So this illustrates our diversification as a company and how we're able to capitalize on current markets and pivot to expanding markets for continued success.

Operator

Your next question will come from the line of Chris Elinghaus from Siebert Williams Shank.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

The discontinued operations number, I'm really thinking from the other segment. I presume that's all Knife River or is anything else included in that number?

David L. Goodin - MDU Resources Group, Inc. - President & CEO

Yes, Chris, I'm going to ask Stephanie Barth here, our Chief Accounting Officer, to maybe walk through a little bit what's included there to help you and others. We know it's a noisy quarter when you think of that, hence, the discontinued operations and also the adjusted earnings on a year-over-year. So Stephanie?

Stephanie A. Barth - MDU Resources Group, Inc. - VP, CAO & Controller

Yes, you bet. Chris, one thing to keep in mind is we only had Knife River's operations for 2 months in 2023 here in the second quarter compared to 3 months last year. And then I would say the other large contributor there would be the separation cost. So some of the transaction-related costs that we incurred for professional advisers as it related to the transaction.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

So the \$14.1 million loss is purely Knife River operational. That doesn't include any Knife River-specific transaction-related expenses?

Stephanie A. Barth - MDU Resources Group, Inc. - VP, CAO & Controller

No, that would actually include the Knife River transaction-related costs.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

Okay. So that's operational plus their share of the initiatives?

Stephanie A. Barth - MDU Resources Group, Inc. - VP, CAO & Controller

Yes.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

Okay. Got you. You gave us the higher utility guidance. But given that Knife River has been spun off and that probably Construction Services is still around for certainly the vast majority of the year and through the heavy construction season. Why did you decide not to do consolidated guidance at this point?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. I would say it really goes back to our point that we started the year, Chris, about being more granular within each of the businesses providing guidance, given the timing uncertainty with Knife River, which grant you is in our rearview of me or now. But I also think for investors, it's good to have more granular knowledge within each of the businesses as we think about them.

And I also would guide you and others to say that we do see ourselves as a future pure-play regulated business at some point. And so certainly, I think as we think about our dividend, as we announced here today as well, that aligns with the payout ratio consistent with regulated pure-play businesses. So we still think the guidance meaningfully represents what we view as a forward look in the business. And I think from an investor point, should be meaningful from their eyes, too. But anything to add to that, Jason, just from a – as you listen to Chris' question?

Jason L. Vollmer - MDU Resources Group, Inc. – VP, CFO & Treasurer

No, Chris, thanks for the question. The only other thing I would add is we also have the retained stake of Knife River as part of the organization here you had as well. And you'll see, I think, through a lot of the disclosures here, and again, as Dave mentioned, it's a little bit of a noisy quarter on some of that. We had some unrealized gains on that kind of throughout the year. That will be -- it's continuing operations.

So even though it's part of Knife River that's been spun out, that will continue to move around a little bit on us. So I think just to kind of put together a consolidated continuing operations number. There's a lot of moving factors there. So we just felt like it was more useful to stick with the segment-specific guidance and kind of stick closer to that or the regulated energy delivery and then the services separately.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

Okay. Dave, you talked about the dividend. You're going to end up probably at -- certainly maybe at the lower end of the new payout target for -- maybe for 2024. Can you give us some thoughts about what you're thinking in terms of how the dividend growth will progress and how you see the payout evolving over time?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. No, spot on question, Chris. Providing a kind of a targeted or expected payout ratio that we just did here today is actually something new for us. I mean thinking prior to our more diversified business model. We always kind of talked about our long rich history, which we reinforced today of 85 years. But certainly guiding folks towards -- actually starting in May, we put out a release that we'd expect our future dividends to reflect more of a pure-play regulated business, consistent with peers in that business. So I mean that's kind of the underpins.

And then as we look to the 60% to 70% payout ratio, I hear your question is, so how do we see that over time? I think that percentage ratio is appropriate. Certainly, that's based on earnings. And also, we would expect our earnings to -- I think rate base growth would be a proxy, if you will, from an earnings on a year-over-year basis. So rate base growth with proper regulatory timely recovery, the 2 should have a relationship. And so that would be my expectation.

And then having said all that, it's obviously up to our Board every quarter as we get the dividend discussion and all these factors come into play. But that would be my expectation that it would have some replication of a proxy to basically rate base growth.

Christopher Ronald Elinghaus - Siebert Williams Shank & Co., L.L.C., Research Division - MD, Principal & Senior Equity Utility Analyst

Okay. One more question for Jeff. Dave sort of touched on this about sort of expecting some pickup in activity from the various legislation. What are you seeing on the clean energy side going forward? Are you seeing incremental business? And is any of that really showing up in the backlog yet? Or is that sort of what's going to be a pretty sizable driver for you going forward?

Jeffrey S. Thiede - President & CEO of MDU Construction Services Group, Inc

I think more of a driver for us going forward. We haven't seen projects directly funded through the Infrastructure Investment and Jobs Act or the Inflation Reduction Act yet in our backlog, but these opportunities are going to provide us a tailwind for the future.

We're very well positioned, Chris, to capture some of these projects due to our experience with this type of work and the services that we provide, highways, bridges, ports and airports and water systems. I mentioned the Kansas City Street Car Extension in the U.S. 69 Expressway. Those are 2 projects we're really excited about. And we're going to build upon our recent project completion and opening of the Kansas City Airport and our continued work at the Portland International Airport.

And of course, our experience in the renewable space, whether it's electric vehicles, EV charging stations and solar work going to put us in a good position for future projects in this area, contract awards, which is going to, of course, contribute to the momentum of our record Q2 backlog and earnings. We've got a great team, Chris, and we're well positioned and those type of projects are on our radar.

Operator

(Operator Instructions)

We'll hear next from Ryan Levine from Citi.

Ryan Michael Levine - Citigroup Inc., Research Division - VP

In terms of the guidance for the regulated business, is there embedded any assumption around an outcome with the pipeline FERC upcoming settlement? Or any color you could share around assumptions or potential upside to your current year guidance based on upcoming regulatory outcomes?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. Certainly, we put those factors in as we best see the future here. I would say one of the other items that, in addition to what items you mentioned would be we expect normal weather. I mean, that's how we look at normal degree days, normal cooling degree days and factor that out throughout the year. And certainly, timely recovery, and then we risk factor that as well. All those come into play with the increased guidance that we're reflecting for the full year.

Ryan Michael Levine - Citigroup Inc., Research Division - VP

Okay. And appreciate the updated color around dividend policy, reflecting payout ratios and rate base growth. I guess on that, a follow-up to that comment, is there any perceived – or is there any potential change that the upcoming potential spin could do to the dividend policy? Or should we look at the reestablished dividend as for to grow from there regardless of the outcome of the upcoming PSG potential transaction?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. No, great question. So part of our purpose again signaling going back to May about we'd expect our future dividend to be aligned with peers as a regulated pure-play business. And that at some point, we look at optimize the value of CSG and a tax advantaged type transaction that we announced here more recently.

So to your point, so we're kind of taking CSG out of the dividend equation as we think about that. Peers in that business often do not have dividends. And so we thought as we think about the underlying long-term kind of future state of the company, I think to your point, we're -- and we're being very specific on target ratio payouts here, and it's specific to the regulated earnings. I think you're spot on as we think kind of a baseline from here to grow.

Ryan Michael Levine - Citigroup Inc., Research Division - VP

Okay. Great. And then in terms of the potential transactions that are being considered, is spinning what's getting the most attention, you're looking at Reverse Morris Trust type transactions? Or any other color around options that may be on the table as the company import evaluate potential alternatives?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. So the short answer would be -- those would be options and there may be more in addition to those in a tax advantage means. I would share that we did a market check, point for this business and just felt where the market was at. And given the relatively low tax basis of this business, we just felt that we could better optimize value of the business by a more tax advantaged separation.

And so I think that should give you some color as to what our thinking here is. And then more as a reminder to you and others, we just went through a full-blown spin with Knife River that, in my humble opinion, I think, created a tremendous amount of shareholder value.

Certainly, we've got some new institutional knowledge that we did not have a year ago specific to a spin. I don't want to overemphasize the spin here, but clearly, we've got some experience there that we can draw on if it's the spin or some other means to find a tax advantage way to separate the high-performing business that it is today.

Ryan Michael Levine - Citigroup Inc., Research Division - VP

Okay. And then last question for me. In terms of upcoming regulatory events outside of the pipeline or decision. Can you refresh us as to the -- where the team is spending their time across all your service territories?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

In my comments, I noted that we've got 3 cases that we're planning for here yet this year. I'll ask Nicole to touch on that and then 1 early in 2024, but she's clearly closer to the activity than I am. Nicole?

Nicole A. Kivisto - President & CEO of Cascade Natural Gas Corp, Intermountain Gas Co & Montana-Dakota Utilities Co.

Yes. So we're right now working through and had filed an all-party settlement in Montana on our electric case there, so that was filed in June, and we're waiting for an outcome from the commission on that one. And then as we look to the remainder of the year, which I think is more of your question, we are intending to file in South Dakota on the electric and gas side in August and then file a North Dakota Gas case later this year. And then as we look ahead to next year, our intention would be to file a multiyear rate case in Washington early next year.

Operator

We'll hear next from the line of Brian Russo from Sdoti.

Brian J. Russo - Sdoti & Company, LLC - Equity Analyst

Should we use the updated energy delivery 2023 guidance as the base year to grow EPS, as you mentioned earlier, or your target to be 5% to 7%, which would be consistent with the rate base growth?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. I'll ask Jason Vollmer to touch on that one.

Jason L. Vollmer - MDU Resources Group, Inc. – VP, CFO & Treasurer

Yes. Thanks, Brian. It's a great question. I think as we look at the dividend and how we are looking at that. So we -- as you mentioned, we increased our regulated energy delivery earnings guidance from what was \$140 million to \$150 million, \$10 million into the new range of \$150 million to \$160 million. So we're excited about that portion of it.

If we think about the guidance, the forward-looking guidance that we're giving now on a targeted payout ratio of 60% to 70%. I think if you think about that, think about the midpoint of the guidance range that we have. If you kind of do the math on that, you'd see that we're right at that kind of 65%, 66% payout ratio for the current year guidance.

So to kind of echo what David said earlier, we really feel like this is a -- based on the current forecast that we see it in a base to grow off of as we look forward. And as we look at the rate base growth, I think you mentioned 5% to 7% or actually in that 6% to 7% range to think about that, so even a little bit higher than that.

As we look back at the midpoint of the guidance range for the utility right now compared to where we were -- or excuse me, the regulated group compared to where we were a year ago, we're actually up in that 11% to 12% range on a year-over-year basis. So we feel very good about the trajectory of where this is going, and we think that on a go-forward basis, it really does set us up very well to be able to grow off the base that we're establishing here today.

Brian J. Russo - Sdoti & Company, LLC - Equity Analyst

Okay. Great. And it seems as if by sometime in 2024, you'll have basically filed and concluded rate cases in nearly all of your jurisdictions, should we -- will there be a time where you'll be earning your allowed ROE? Or will there always be some sort of regulatory lag just based on test years, et cetera? And is there any sort of like natural inherent lag in the utility businesses?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Yes. Brian, I'll ask Nicole again, maybe with some details, but kind of on a macro level, if we think about overall CapEx at her business along with WBI, we're forecasting \$2.5 billion over the next 5 years, which is in excess of depreciation. And so kind of by its very nature, there is going to be some regulatory lag there, if you think of it that way.

But anything to add to that, Nicole, I know we're tightening up that lag, but at the same time, because we're a growing rate base at that 6% to 7% that Jason noted and we've touched on earlier, there will be some inherent lag in there, some jurisdictions longer than others based on forward-looking or rear-looking test periods. Anything to add, Nicole? I didn't want to take the whole question, but I kind of did.

Nicole A. Kivisto - President & CEO of Cascade Natural Gas Corp, Intermountain Gas Co & Montana-Dakota Utilities Co.

Yes. No, I think you summarized that well, Dave. So just what he said, I mean, the punchline is at the rate of growth that we are achieving and expecting to get, we are going to have some inherent lag. So we've got the general rate case process that we do in all of our states, and we'll continue to monitor our returns and file as appropriate.

The other thing that I would add to Dave's comments that would be in certain of our states, we have the ability to use tracker mechanisms. So in -- as an example, in the state of Washington, we have a pipeline tracker, in the state of Minnesota, we have a pipeline tracker. In the state of North Dakota, we have various tracker mechanisms on the electric side where we can do annual filings to reduce our regulatory lag on certain of our investment opportunities. So we're going to do those where we can.

And then manage our filings according to growth in the other states where we're falling underneath are allowed. So I guess the punchline is, with the growth rate we have, we will continue to have to be in the regulatory arena.

Brian J. Russo - Sdoti & Company, LLC - Equity Analyst

Okay. Great. And then just on CSG. Just on -- based on your operating statistics, it looks like nearly all of the revenue growth is coming from the electrical and mechanical side of the business where transmission and distribution was flat in this June quarter versus a year ago and even when you look at the year-to-date of '23 versus 2022.

Can you just kind of discuss what's going on there? I see the backlog is up on T&D, but it's down on E&M. So I'm just -- I'm curious what kind of dynamics you're seeing in those 2? What are, I would say, distinctly different end markets?

David L. Goodin - MDU Resources Group, Inc. -- President & CEO

Sure, Brian. Jeff, can you add some color on that as we think about that on a year-over-year basis?

Jeffrey S. Thiede - President & CEO of MDU Construction Services Group, Inc

Yes, absolutely. Our T&D sector, most of the work is through our MSAs. And as I mentioned earlier, we've got updates with our MSAs. We're going to see that reflection of earnings going forward as we caught up with the updated labor material, fuel and equipment.

But then on our projects in the T&D space that contribute to our backlog are most notably the projects that I identified before, the Kansas City Street Car Extension and U.S. 69, but also our wildfire mitigation that we're involved in, in addition to the undergrounding for electrical services, a lot of joint trenching with gas and communications.

And we're doing this work, of course, for our customers in Southern California and other California, Pacific Northwest, Rocky Mountain Midwest. But mostly, we're seeing that emphasis in New or Northern California from our utility customer, and we have tremendous experience with and a relationship with.

So some of it is timing and some of it is the CapEx and the bids that are released, which is beyond our control, but we're incredibly well positioned to be able to capture this work on the T&D side. And on the E&M side, we're seeing some of these projects complete in Las Vegas, but we're also fighting. We're involved in other projects that are on our radar that are significant in that market.

And of course, we've expanded into Arizona because a customer asked us to be there, and we're seeing significant contribution within that region for us. And there's another project that we're looking at in that area that we hope to report in future calls here that are going to be a contributory factor. So the work still out there is still available and we're well positioned with our resources to be able to get the best of it and continue our success.

Brian J. Russo - Sdoti & Company, LLC - Equity Analyst

Okay. Great. And then also just the way the overall CSG business mix has evolved over the years. It seems that the E&M side of the business has been growing at a faster rate and maybe it's about 2/3 to 3/4 of the topline. But given the margins are lower, relative to T&D. I'm just curious, do you think you're going to get back to your historical say, pre-inflationary type margins with the new backlog over the next 12 or 24 months?

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Jeff, do you want to take that one?

Jeffrey S. Thiede - President & CEO of MDU Construction Services Group, Inc

Absolutely. We want both businesses to grow. Limiting factor is really people and labor, very difficult on the T&D side because the level of available qualified labor, but we have support of our companies through our CapEx program through our expansion. We built a brand-new facility in Kansas City for our T&D company there, and that company is growing.

And then, of course, the work that we see in the future with the undergrounding of the electrical services, I believe, is going to help build that backlog and that balance.

Meanwhile, it would be expansion of the opportunities in the mission-critical market, and we have a couple of health care projects that are significant, 1 in the Mid-Atlantic, the other 1 in Ohio. But we're seeing the faster growth than the opportunities. And so we're going to capture the ones that best fit us on our resources and with the customers that align with our values where we could be most successful.

Operator

(Operator Instructions)

Also, please note, the webcast can be accessed at www.mdu.com under the Investor Relations heading. Select Events and Presentations and click Q2 2023 Earnings Conference call. After the conclusion of the webcast, a replay will be available at the same location just a moment. At this time, there are no further questions in the queue. I would like to turn the conference back over to management for any additional or closing comments.

David L. Goodin - MDU Resources Group, Inc. – President & CEO

Thank you, Lynette, and thank you all for taking time to join us on our second quarter earnings call. As you heard earlier, we are optimistic about our growth opportunities and our future regulated energy delivery projects, and encouraged by the strong demand and performance of our construction service business.

We certainly look forward to connecting again as we pass progress through 2023. We thank you again, and we appreciate your continued interest and support of MDU Resources. And with that, I'll turn it back to you, Lynette.

Operator

Thank you. This concludes today's MDU Resources Group conference call. We thank you all for your participation. You may now disconnect.

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