

Electric Utilities

WEEKLY ANALYSIS

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Things We've Learned This Week

Our Take: As utilities underperform for a third week in a row, [we reiterate our view that the sector is fairly valued](#) vs the S&P 500 based on correlation to the 10-year yield and the CS forecast for a 2.8% yield by yearend. While this may be a somewhat more bullish view than some investors concerned over the potential for rising rates, it is nevertheless more bearish than other sector views as highlighted this week by our CS Portfolio Strategist Lori Calvasina in her [2H17 Outlook piece](#).

VST announced the purchase of a 1.1 GW CCGT in fuel-advantaged (discounted Permian gas) West Texas for \$350M (\$332/kW) plus a spark spread-based earn out. This would be consistent with our [prior views of ~\\$300/kW](#) of market value for EXC's two new-build CCGTs nearing completion this summer in North and East Texas at a cost of ~700/kW (broke ground in 2015). VST also estimated its purchase price at a 60% discount to new construction, implying ~\$830/kW. Also note that in May, VST management opined that West Texas Waha hub discounts are viewed as temporary, with the advantage likely to erode once three new pipeline projects are finished to move gas East and South out of the basin.

We also spotlighted [Montana's apparent attempt to deregulate its power market](#) by extending regulatory reform of Qualifying Facility renewable contracts to utility and other IPP assets. A set of recent orders would impart 5-year price reopeners for all new long-term contracts, even new utility generation, a condition that would significantly stress NWE's 7%-10% total return targets. However, with NWE currently trading at a 3% discount to peers (2018 P/E), we see much of risk already priced in and reiterate Neutral. Going forward, we are looking for regulatory treatment of fuel recovery this month, with particular emphasis on the baseline fuel cost to be set in rates under the recently adjusted power cost recovery tracker under HB 193. [As we have previously noted](#), NWE is considering accelerating its plan to file a full ratecase next year into the Fall in the event of poor rate treatment on the power supply assets (as transmission and distribution assets are under-earning but offset with earnings from power gen assets).

Finally, with France planning to end sales of gas and diesel cars by 2040, we update our thoughts on electric vehicles and their ability to reduce carbon emissions in *some* countries. France is one of only a handful of countries with >50% of electricity generated from carbon-free sources (the US is only ~33%).

Save the Date: We will be hosting meetings with regulators in accordance with the NARUC 2017 Summer Policy Summit on [Monday July, 17](#). Tentative commissioner attendance from the following states; OH, WA, CO, MO, MI, GA, AZ, DC, SC, WI, TX, MT, and NV. Please contact the team or your CS Salesperson to sign up; full agenda to follow.

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Figure 1: CS Utilities Catalyst Calendar – 2017

Company	Ticker	Description	Timing	Note
Exelon	EXC	Testimony due in ComEd FRP Proceeding	6/27/2017	ICC recommended \$99.1M inc., 6/28
Dominion	D	CT Legislative Session End - last day for Millstone legislation	6/30/2017	Special Session June 30th*
Black Hills Corp	BKH	Renewable RFP Issuance - Approval at year-end	2Q17	Issued June 23rd, up to 60 MW
Northwestern Corp	NWE	MT Gas Ratecase Final Decision	7/1/2017	Expected
Exelon	EXC	Rebuttal testimony due in ComEd FRP Proceeding	7/21/2017	\$99.9M requested, \$99.1M recommended
ALL Regulateds		FOMC July Meeting	7/26/2017	
Black Hills Corp	BKH	Cost of Service Gas Filing	2Q17/3Q17	Previously 1H17
DTE Energy	DTE	NEXUS Approval	1H17	
Exelon Corp	EXC	Pepco Electric DC Ratecase Final Decision	7/31/2017	Expected
Exelon Corp	EXC	NY ZEC Decision	July, 2017	Expected
Duke Energy	DUK	Appeals Decision RE: Constitution Pipeline Water Quality Certificate	Mid-2017	
Eversource	ES	ISO-NE Midyear Analysis, expected to support ANE	Mid-2017	
Multiple	CMS, DTE	Michigan PSC - Commissioner Eubanks Term Expires	July, 2017	(I)
CMS Energy	CMS	Gas ratecase expected decision	8/1/2017	Expected
Eversource	ES	Hearings in NSTAR Electric and WMECO ratecases	August, 2017	Previously June 2017
Southern Company	SO	Kemper IGCC ratecase filing - in-service date pending	August, 2017	Potential settlement due 8/20
Southern	SO	Sanmen (China) AP1000 Reactor - Fuel Loaded	Summer 2017	at some point in the summer
CMS Energy	CMS	MPSC Commission Order on Palisades Securitization	August, 2017	
ALL Regulateds		FOMC September Meeting	9/20/2017	
Multiple	DUK, SO, D	ACP Final Environmental Impact Statement	9/28/2017	Sept. 28 is the latest date
Eversource	ES	Northern Pass NHSEC Decision	9/30/2017	
Dominion	D	Rider BW, U-2 filing	October, 2017	Expected
Spire	SR	Mobile Gas 4-year review of RSE Filing	October, 2017	
ALL Regulateds		FOMC October/November Meeting	11/1/2017	
ALL Utilities		EEl Financial Conference	11/5/2017	Capex/Guidance Updates
Duke Energy	DUK	Lee CCGT Completion	November, 2017	
Spire	SR	STL Pipeline Milestone; FERC Final Order	November, 2017	Assuming FERC quorum
Eversource	ES	WMECO and NSTAR Electric Ratecase Decisions	November, 2017	Expected
ALL Regulateds		FOMC December Meeting	12/13/2017	
Dominion	D	Cove Point In-Service	2H17	
Black Hills Corp	BKH	Sale of Non-Core Oil and Gas Properties Completed	2H17	Complete by YE
Northwestern Corp	NWE	Colstrip Litigation Resolution	2H17	Expected 'end of year'
Northwestern Corp	NWE	FERC/DGGS Resolution	2H17	Second half at the earliest'
DTE Energy	DTE	NEXUS Pipeline completed	4Q17	Before year end
Spire	SR	Missouri PSC - Commissioner Stoll Term Expires	December, 2017	(D)
Exelon	EXC	Deadline for Decision in FRP proceeding	December, 2017	
Black Hills Corp	BKH	COSG Resolution	2017	
Eversource	ES	PSNH Generation Divestiture	2017	Late-2017
Eversource	ES	Massachusetts Solar Filing Facility Completion	2017	YE 2017
Black Hills Corp	BKH	Colorado IRP Approval	2017	Expected by YE
Black Hills Corp	BKH	IRP for South Dakota and Wyoming	2017	
DTE Energy	DTE	IRP Filing in Michigan	2017	"later this year", 4q16 call

Source: Company data, Credit Suisse

- Cleaning the slate – Westinghouse looks to exit bankruptcy in 1Q18.** Westinghouse's CEO Jose Gutierrez said this week that the company expects to exit bankruptcy with a new owner by the end of 1Q18, with a formal business plan and financial details ready in July (for potential bidders). Mr. Gutierrez also stated that the company has received interest from a number of potential buyers, without naming anyone specifically. The buyer will need approvals from various entities including: bankruptcy Court, the Nuclear Regulatory Commission (NRC), and the Department of the Treasury's Committee on Foreign Investment. Westinghouse reiterated that work has continued uninterrupted at the new units at Vogtle and V.C. Summer under the new agreement (**SCG, SO**).
- Starting the 45-day countdown.** The Mississippi Public Service Commission (PSC) voted 3-0 on Thursday to give SO 45-days to file a settlement proposal to operate Kemper solely as a CCGT. The Commission has stated that any potential proposal should: 1) eliminate ratepayer responsibility for the gasifier and associated equipment, 2) alter the plant's operating license to run only as a CCGT, and 3) not increase customer rates. As a result of the decision to halt operations of the gasifiers SO injected \$1B of capital into Mississippi Power, in-line with we had expected. Mississippi

Power used a majority of the \$1B equity injection to pay down debt, including a \$591M loan from SO parent company.

- **Access...denied–Access Northeast officially halted.** This week, Enbridge (**ENB**) notified FERC that it is planning on halting the development of its proposed Access Northeast pipeline (\$3.2B). The project is owned by Enbridge, Eversource (**ES**) and National Grid (**NGG**) and would have increased gas capacity in the region by 925,000 Dth/d. Earlier this week Enbridge noted that the halting of the project was only temporary and stated that "once we work through the legislative support, we'll be able to reengage the FERC filing process and be back on track"
 - **5/28 Weekly: More fuel security concerns in the Northeast.** ISO New England (ISO-NE) announced that it is conducting a study to examine the wintertime challenges to power plants' ability to procure fuel required to generate power in the northeast. The study will examine the performance of generating resources under a variety of different scenarios that could impact grid reliability for the winter of 2025. In the memo announcing the study the ISO stated that, "the regional power system is increasingly dependent on natural gas for power generation...the capacity of the region's natural gas infrastructure is not always adequate to deliver all the fuel needed for both heating and power generation during winter; the region has limited dual-fuel generating capability with emissions restrictions on burning oil." ISO-NE also highlighted that the study *will not* focus on the impact of any possible gas pipeline expansions or specifically identify the need for new gas pipelines or infrastructure (**ES**).
- **Scaling back–MD PSC recommends lower than requested rate increase.** Last week the Maryland Public Service Commission (PSC) filed their recommendation in Pepco's electric ratecase (Case # 9443) recommending a rate increase of \$24.9M, or 3.7%, based on an ROE of 9.38%, equity ratio of 50.15% and \$1.632B of ratebase. This compares to the company's revised request for a \$68.6M rate increase (10.1%) at a 10.10% ROE, 50.15% equity ratio and \$1.694B of ratebase. A final decision on the rate case is expected in October.
- **The last man standing – FERC down to one.** FERC Commissioner Colette Honorable officially stepped down on June 30th concluding her 2.5 year term on the Commission, leaving Commissioner LaFleur (D) as the last remaining Commissioner at FERC. Commissioner Honorable was nominated by President Obama in 2014 and if she had chosen she could have stayed on through the end of the year while the open seats on the Commission were filled. President Trump's three nominations are currently pending Senate Confirmation: Robert Powelson (R), Neil Chatterjee (R), and Richard Glick (D).
 - **6/25 Weekly: Filling up FERC – Glick in the lead for minority pick.** It has been widely reported that Rich Glick (D) is expected to be nominated to the federal energy regulatory commission (FERC) to replace Commissioner Honorable (D) when her term expires on June 30th. If no replacement has been confirmed by her term expiration, Commissioner Honorable would be allowed to remain in her seat through a grace period which would run through the end of the current Congressional session (November/December). Glick currently serves Staff on the Senate Energy and Natural Resources committee. White House sources have been quoting saying that it's "agreeable to advancing the nomination and is processing his paperwork" and that "[Rich Glick] is definitely it (the nominee)." Prior to working on the Senate energy committee, Glick worked as VP of government affairs at Iberdrola, as a lobbyist for the wind industry, and previously served as a senate aide to Senator Dale Bumpers of Arkansas (D). It is expected that the nomination of a

Democrat would help speed up the Senate confirmation of President Trump's other two FERC nominees, Robert Powelson and Neil Chatterjee, whose confirmations remain pending on the Senate Floor (they passed the Senate energy committee on June 6th).

- **TMI is 'seriously' planning to close.** This week, Exelon (**EXC**) officially notified the Nuclear Regulatory Commission (NRC) of its plans to close Three Mile Island (TMI) around September 2019. In a statement, EXC said that TMI "is unprofitable and has lost more than \$300M over the past five years despite being one of EXC's best-performing plants." EXC continues to push for a ZEC program similar to IL and NY to keep the plant open; no legislation has currently been proposed.
 - **6/25 Weekly: See at least \$0.05 of upside from TMI upside (or more if they get a PA ZEC).** EXC has announced their intention to retire the Three Mile Island (TMI) merchant nuclear facility around September 2019. As we highlighted in our recent EXC note ([EXC: Goals Achievable Even Through ZEC Appeals](#)), legislation in Pennsylvania to support a nuclear subsidy of some kind is not yet in the works and could face opposition from a relatively strong oil & gas industry in the state.

Recent Excerpts:

- **NWE: Montana Drops a Goose Egg (7/6):**

Is Montana once again sliding toward deregulation? On June 22, the Montana Public Service Commission (MPSC) ordered to cap the length of NWE's long-term power contracts to a maximum 10 years, with a contracted price reopener at 5 years. While the order was primarily aimed at reducing the extraordinary length of Qualifying Facility (QF) contracts that have typically extended above-market rates to 25 years, the MPSC appeared to extend the policy much further, deciding "to apply this standard across the board, holding all energy projects, whether they are owned by the utility or independent developers, to the same standard. Vice-Chairman Travis Kavulla stressed, "What's good for the goose is good for the gander." Chairman Johnson agreed, stating "Our actions will help to mitigate the risk associated with relying on long-term price forecasts that are at best imperfect in the setting of rates customers pay for electricity." Commissioner Koopman: "It's not the role of the Commission to guarantee anyone's business success."

- **Highlighting: CS Portfolio Strategist Remains Underweight Utilities (7/6):**

Highlighting: Our Portfolio Strategist Lori Calvasina reiterated her Underweight view on Utilities in her 2H17 Utilities Outlook piece on the following basis:

- *She notes that ETF flows have been negative, that valuations look expensive relative to the broader market on forward P/E, our technical strategists are cautious, and she believes the sector is likely to underperform if interest rates move up later this year.*
- *She believes earnings momentum in the utility sector has been lackluster, despite being strong in most other sectors in recent months.*
- *In her positioning update, she feels the sector looks a bit under owned in small cap, but a bit over owned in large cap with hedge fund exposure at the high end of its range.*

- **Alternative Energy Weekly: Renewable Roundup (7/7):**

Electric storage and electric vehicles dominated headlines this week as corporates and countries get comfortable with disruptive potential of the technology. Solar stocks were down 3-5% this week showing correlation with weak oil prices.

- **Last Week's Things We've Learned This Week (6/30):**

Our Take: *Utilities underperformed another 1.7% for the second week in a row (3.4% over the past month) as the 10-Year sold off a bit on what appears to be increased caution over the possibility of a somewhat more aggressive quantitative tightening following the June FOMC meeting. We nevertheless continue to see the group as fairly valued at a 2% premium forward P/E vs the S&P 500 based on historic correlation to the CS forecast for a 2.8% 10-Year yield by year-end. We also note more dovish comments on inflation in recent weeks, which we believe sets a more bullish backdrop to our yield-oriented sector. Investors we've spoken to this week remain broadly concerned about record-high utility P/Es and continue to debate which stocks are likely to hold up better in a possible rising rate/underperforming utility world, should that come to pass. We continue to cite undervalued names already trading at significant discounts with a positive catalyst calendar ahead, with EXC remaining our top pick as clarity builds around its ZEC legal cases. While SO also trades at a discount, we continue to rate it Underperform ahead of equity issuances that might be needed for its Kemper clean coal plant and possibly its Vogtle new nuclear project as well. We also see SO's 5% EPS growth target as significantly at risk in light of coming dilution.*

Companies Mentioned (Price as of 07-Jul-2017)

Amazon com Inc. (AMZN.OQ, \$978.76)
Black Hills Corp (BKH.N, \$68.2)
CMS Energy Corp (CMS.N, \$45.75)
Calpine (CPN.N, \$13.42)
CenterPoint Energy Inc (CNP.N, \$27.32)
Consolidated Edison (ED.N, \$80.53)
DTE Energy (DTE.N, \$105.26)
Dominion Energy (D.N, \$75.79)
Duke Energy (DUK.N, \$83.42)
Dynegy Corporation (DYN.N, \$7.67)
EQT Midstream Partners, LP (EQM.N, \$76.3)
Enbridge Inc (ENB.N, \$39.81)
Entergy Corp (ETR.N, \$75.79)
Eversource Energy (ES.N, \$60.07)
Exelon Corporation (EXC.N, \$35.58)
NRG Energy (NRG.N, \$16.24)
National Grid (NG.L, 934.7p)
NiSource Inc. (NI.N, \$25.32)
NorthWestern Energy (NWE.N, \$60.3)
SCANA (SCG.N, \$65.02)
Sempra Ener (SRE.N, \$110.53)
Southern Co. (SO.N, \$47.36)
Spire Inc. (SR.N, \$69.95)
Unitil (UTL.N, \$48.7)
Vistra Energy (VST.N, \$16.44)
Whole Foods Market (WFM.OQ, \$42.0)
Xcel Energy (XEL.N, \$45.69)

Disclosure Appendix

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