**NORTHWESTERN CORPORATION (NYSE: NWE)**

**Q217 Disappoints, Reducing Estimates, MPSC Risk Still Too Great**

- NorthWestern reported a 22.8% decline in Q217 recurring earnings to $21.8 million, $0.45 per share compared with $28.2 million, $0.58 per share in the year ago second quarter.

- NorthWestern’s Q217 recurring EPS results missed our $0.61 estimate and consensus expectations of $0.62.

- Earnings were lower due to a $11.5 million decline in gross margin (excluding items covered by trackers and other offsets), largely a result of the absence of the Q216 deferred revenue recognition issue, and higher operating costs.

- Management noted that some of this cost inflation timing that adversely affected second quarter results should be a lesser headwind in 2H17. On the call, management also noted that credit rating pressures could require new equity.

- We reiterate our Hold investment rating and $64.00 target price on NorthWestern Corporation (NYSE: NWE) on July 27, 2017 at a price of $59.29.

- While the decline in NWE shares of late has led to a nearly 11.5% total return to our target price, we are not raising our investment rating at this time. The risk profile of the company is simply too great.

- Take note MPSC, the required rate of return on NWE equity is closer to 15.0% than 9.55%, write it down, we said it.

- Please see our revised earnings estimates for 2017-2019 below and our 20 Questions for Management on page 14.

**Market Data**

- Price: $59.29
- Market Cap: $2,874
- Indicated Dividend: $2.100
- Div. Payout: 61.6%
- Debt/Total Capital: 54.2%
- Book Value: $35.26
- Price-to-Book: 1.68x
- LT EPS Growth: 3.8%
- 52 Week High/Low: $63.86/$53.85
- Avg. Daily Volume: 322,579

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**EPS Outlook**

<table>
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<tr>
<th>Year</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
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<tr>
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<td>2015</td>
<td>Actual</td>
<td>$1.09A</td>
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<td>2016</td>
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<td>$0.92A</td>
<td>$0.58A</td>
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<tr>
<td>2017</td>
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<td>Prior</td>
<td>$1.17A</td>
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<td>2018</td>
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<td>$0.67E</td>
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<tr>
<td>2019</td>
<td>Current</td>
<td>$1.30E</td>
<td>$0.54E</td>
<td>$0.78E</td>
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<td>$1.32E</td>
<td>$0.61E</td>
<td>$0.65E</td>
<td>$1.09E</td>
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**Notes:** 2013 recurring EPS excludes Q3 -$2.8 mil p-t, -$1.7 mil a-t, -$0.04 PPL hydro acq. transaction costs, incl. $1.2 mil prior period DSM, -$3.5 mil p-t, -$2.1 mil a-t, -$0.04 PPL hydro acq. transaction costs, incl. -$0.6 mil prior period DSM. 2014 excludes -$9.5 mil a-t, -$0.24 Hydro transaction costs, $18.5 mil, $0.47 tax benefit. 2015 excludes Q2 $20.8 mil p-t, $12.8 mil a-t, $0.27 insurance recovery benefit, $3.75 mil a-t, -$0.08 Q4 adjustment. 2016 excludes Q2 -$10.3 mil p-t, -$5.2 mil a-t, -$0.13 MPSC Colstrip/generation planning cost disallowances, Q2 $14.2 mil p-t, $8.7 mil a-t, $0.18 IRAM deferred rev. recognition for prior periods, -$1.3 mil a-t, -$0.03 Colstrip disallowance chg., Q3 $12.5 mil a-t, $0.26 repairs tax deduction tax acctg. chg. for prior periods. 2017 excludes capital leases.

**P/E**

<table>
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<tr>
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<th>2013A</th>
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<tr>
<td>P/E</td>
<td>14.5x</td>
<td>14.7x</td>
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**Div. Payout**

<table>
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<tr>
<th>Year</th>
<th>2011A</th>
<th>2012A</th>
<th>2013A</th>
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<tbody>
<tr>
<td>Div. Payout</td>
<td>58.4%</td>
<td>62.8%</td>
<td>59.4%</td>
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**PLEASE SEE PAGES 15-17 FOR IMPORTANT DISCLOSURES, REG AC ANALYST CERTIFICATION AND DISCLAIMERS.**

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Q217 Earnings/Call

NorthWestern Corporation reported a 22.8% decline in Q217 recurring earnings to $21.8 million, $0.45 per share (yes, $0.45!) compared with $28.2 million, $0.58 per share in the year ago second quarter. There were no non-recurring items recorded in the latest quarter. However, recurring earnings in Q216 exclude a $14.2 million pre-tax, $8.7 million after-tax, $0.18 per share LRAM deferred revenue recognition for prior periods and a $2.1 million pre-tax, $1.3 million after-tax, $0.03 per share Montana Public Service Commission (MPSC) Colstrip outage/generation planning disallowance. NorthWestern’s Q217 recurring EPS results missed our $0.61 estimate and consensus expectations of $0.62 badly.

Earnings were lower due to a $11.5 million decline in gross margin (excluding items covered by trackers and other offsets), largely a result of the absence of the deferred revenue recognition issue. Cooler temperatures were near a neutral impact in the quarter. Higher operating expenses (mostly O&M, property taxes and DD&A) also increased $8.5 million pre-tax of which +$4.3 million was property taxes. O&M alone increased $2.6 million, or +3.6%. Management noted that some of this cost inflation timing adversely affected second quarter results and should be a lesser headwind in 2H17.

Cooler temperatures, particularly in Montana, aided second quarter results ever so slightly. Montana heating degree days increased 12.1% compared with Q216 to only 92.6% of normal. While natural gas sales/gross margin increased, lower electricity sales/margin offset the improvement on the natural gas side of the house. Overall, management estimated that below normal weather reduced Q217 earnings by $1.2 million after-tax, -$0.03 per share. While heating degree days increased in South Dakota about 6%, heating degree days remained 94% of normal and Nebraska was actually 1% warmer than Q216 and only 89% of normal. Recall however, the 80% rules, electricity is roughly 80% of gross margin and over 80% is derived from the Montana service area, so the relative weakness in natural gas in South Dakota and Nebraska were less critical to Q217 results as Montana was relatively stronger year-to-year.

Retail kilowatt hour electricity sales declined 0.8% while retail natural gas dekatherm sales increased 8.3% for the quarter. Electric revenues declined $14.5 million, -5.8% while natural gas revenues increased $5.3 million, +11.9% as a result of the closer to normal weather. Average electric and natural gas retail customers both increased 1.2% compared with Q216.

Q217 Conference Call

Management reiterated its 2017 EPS guidance of $3.30-$3.50. Management noted some unusually high operating costs, particularly property tax expense, in 1H17 that it expects to be less challenging in 2H17. The weather has been very hot in July and the company has implemented cost controls again to help meet 2017 guidance. Management appears bent on meeting the guidance range, in our view. Debt-to-capitalization declined below the 55.0% level for the first quarter in awhile to reach 54.8%.

The company’s definition of recurring EPS in the second quarter of $0.47 included the adjustment for $0.03 per share of cooler than normal weather and a rounding of the diluted EPS of roughly $0.01 per share. As we include actual weather in our estimates, it appears that the middle portion of the range is increasingly likely for the year, in our view. The company’s latest guidance reflects 48.6 million average diluted shares, normal weather and a range of anticipated effective income tax rates of 7%-11% (recurring). The company maintained its CAPEX guidance through 2021 but noted that about $100 million of the CAPEX budget still includes new Montana generation. The question now is will the company reduce future CAPEX due to recent MPSC generation rule changes or redeploy that capital.

NorthWestern CFO Brian Bird maintained the company’s expectations for attaining the lower–end of its 7%–
10% annual total return target due to the lower capital expenditures and recent adverse regulatory decisions and the delays regarding new generation investment proposals but noted that cost controls should allow the company to remain within the range. This implies intermediate-term EPS growth for NorthWestern of only about 3.5%, in our view. Management previously noted that it increased the 2017 dividend growth to 5.0% partially to compensate for the lower prospective EPS growth. Management noted that MPSC planned changes to power cost recovery and property tax trackers could make earnings growth even more challenging going forward.

Management indicated its plan for a Montana electric rate case filing will be postponed until May 2018 back in April. The company is hoping that proposal holds up as the MPSC will meet Friday morning to discuss power cost recovery mechanism options that could result in an adverse ruling on the rate case timing. While management remains optimistic on the regulatory front, we did not hear any solutions or anything to give us optimism at all. Finally, management noted that credit rating downgrades due to the agencies’ deteriorating perception of the regulatory climate in Montana and a potentially more challenging power cost/property tax recovery outlook could put pressure on the company’s FFO/debt ratio and require new equity.

Earnings Estimates/Growth Outlook

In the absence of new natural gas acquisitions, depletion should prove a modest headwind for company annual results. Low electricity prices are also proving to be a drag on transmission revenues of late. Assuming a return to more normal weather in 2017, we expect most of the -$0.19 per share drag on 2016 earnings should dissipate this year. With much improved weather and particularly strong Q117 results, 2017 is looking mildly encouraging, in our view. Longer-term, the company has reduced CAPEX budgets through 2021 as a result of regulator resistance to new generation investment proposals to reduce the extreme short position the company maintains. Ultimately, the company’s reserve margin issue will be addressed, providing significant new growth opportunities. However, new large generation investments are postponed for now pending a better regulatory response. We expect long-term (5-year CAGR) EPS growth of 3.8% absent any generation investment opportunities. While we are reducing our estimates somewhat, our longer-term EPS growth rate was unaffected materially. However, our weather-normalized growth rate is closer to 2.5%. Of course, this suggests that the total return profile for NWE could be closer to 6.0% than the low-end of the 7%-10% management target.

Recent material adverse rulings and opinions from the Montana Public Service Commission (MPSC) over the past several years are a concern for us. The MPSC previously eliminated the company’s Lost Revenue Adjustment Mechanism (LRAM) in September 2015. The decision reduced NorthWestern’s annual revenues by about $7 million. The reduction of authorized natural gas production rates and the recent Colstrip disallowances have also materially affected company financial results in recent periods. Of late, the MPSC

Exhibit 1: Recurring 2017 Segment Estimates

<table>
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<tr>
<th>Operating:</th>
<th>Q1/17A</th>
<th>Q2/17A</th>
<th>Q3/17E</th>
<th>Q4/17E</th>
<th>FY17E</th>
<th>Yr/Yr</th>
<th>% of Total</th>
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<tbody>
<tr>
<td>Reported:</td>
<td>$1.17</td>
<td>$0.45</td>
<td>$0.75</td>
<td>$1.04</td>
<td>$3.41</td>
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<td>9.7%</td>
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<td>Electric Utility</td>
<td>$0.70</td>
<td>$0.49</td>
<td>$0.88</td>
<td>$0.70</td>
<td>$134.55</td>
<td>$1.61</td>
<td>-52.4%</td>
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<tr>
<td>Gas Utility</td>
<td>$0.42</td>
<td>$0.00</td>
<td>$0.12</td>
<td>$0.32</td>
<td>$29.98</td>
<td>$0.62</td>
<td>34.7%</td>
</tr>
<tr>
<td>Corp. &amp; Other</td>
<td>$0.05</td>
<td>-$0.04</td>
<td>-$0.01</td>
<td>$0.02</td>
<td>$0.58</td>
<td>$0.01</td>
<td>-46.9%</td>
</tr>
<tr>
<td>Total Diversified</td>
<td>$0.05</td>
<td>-$0.04</td>
<td>-$0.01</td>
<td>$0.02</td>
<td>$0.58</td>
<td>$0.01</td>
<td>-46.9%</td>
</tr>
<tr>
<td>Total</td>
<td>$1.17</td>
<td>$0.45</td>
<td>$0.75</td>
<td>$1.04</td>
<td>$3.41</td>
<td></td>
<td>9.7%</td>
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<tr>
<td>Recurring Earnings</td>
<td>$56.567</td>
<td>$21.830</td>
<td>$36.500</td>
<td>$50.750</td>
<td>$165.647</td>
<td></td>
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Source: Williams Capital estimates, NorthWestern

While 2017 should be a good earnings year due to better weather, the longer-term outlook is uncertain.
has objected to NorthWestern’s new generation proposals despite a reserve margin deficit of nearly 30% and actively worked with the legislature to adversely modify a property tax expense tracking mechanism. The MPSC has taken to making unusual proclamations of how evil utilities (not just NorthWestern) are in public press releases. It remains rogue regulatory mayhem up there! We are not sure what has the MPSC in a punitive mood in relation to the company, but it certainly does not bode well for the company’s regulatory relations, in our view. It certainly does not bode well for the company’s Montana base electric rate case in 2018 or the ability of the company to receive approval for future generation resource filings with this unpredictable commission, in our opinion. The dubious Montana regulatory climate is a considerable negative for NorthWestern’s growth potential, ability to reduce the company’s (and customers’) exposure to the wholesale power market, and is a material detriment to the company’s cost of capital, in our view. What was once an up and coming regulatory environment appears deeply flawed at this point, in our view.

On a potentially positive note (although not currently looking good at all), NorthWestern filed its biennial Montana electricity supply resource procurement plan with the Montana Public Service Commission (MPSC) on April 1, 2016. NorthWestern’s filing suggests significant capacity shortfalls developing (including the Boardman and Centralia retirements) in the region and notes the company’s current -28% planning reserve margin, -338 megawatt (MW) shortfall. With load growth, the company expects the company’s Montana capacity shortage to grow to 688 MWs in later years. While the company does not address it in this filing, it will also ultimately need to establish a reserve margin of about 15% at some point. Effectively, the company’s filing outlines its plan to meet its minimum load over the next 10 years, establishing a neutral reserve margin by 2028. To meet this goal, the company developed a specific optimal set of generation projects to add 689 MW of new generation capacity. The initial cost estimate for the 689 MWs is about $1.3 billion. The company also notes 86 MW of additional hydro capacity projects as opportunities to add additional capacity without estimating timing or costs. The figures exclude the capacity and costs associated with another 86 MW of hydro expansion opportunities. The company also notes that it retains significant flexibility to adjust to actual load growth and regional developments in its plan given the phased stages of plant additions envisioned through 2029. NorthWestern’s capacity plan is a significant enhancement to the company’s future growth outlook, in our view. We expect the company to provide further details of its plan and CAPEX as the year progresses. Unfortunately, the vast majority of the generation capital spend is back-end loaded for after 2020, providing little support for our near-term outlook. Also, given the current mood of the MPSC, it is difficult to gauge the ultimate outcome of the company’s plan to improve its generation capacity and reserve margins. While regulatory opposition to what appears to be a logical plan has derailed any near-term opportunity for the company, the outcome is inevitable in the long-run.

Our enthusiasm for the company’s growth prospects has largely been derailed by the MPSC. While planned company CAPEX still will exceed D&A by almost 100% over the next five years, the considerable growth potential for the company related to generation needs are not a near-term issue. Rate base growth could be high depending on the details of new generation plans/timing. The 2020-2030 period could be a very exciting time for the company’s growth due to significant generation investments needed. We note that the extension of bonus D&A and wind tax benefits in 2015 and current MPSC “dynamics” could significantly affect the company’s eventual capital plans. Fortunately, in the absence of major acquisitions or more robust generation investment plans, we also do not expect material equity dilution to affect EPS growth through 2021. In the meantime, low growth appears more likely for the company. NorthWestern said as much on the Q416 earnings call. Our 5-year EPS growth rate estimate for NorthWestern of 3.8% looks somewhat sluggish compared with peers, in our view. Regulatory treatment of power cost recovery and property trackers could affect our growth outlook still as well.
Considerable uncertainties remain for the company related to potential new Montana generation, natural gas production acquisitions/depletion, distribution and transmission reliability plans (DSIP & TSIP), and environmental compliance capital requirements, in our view. The sometimes Machiavellian machinations of the MPSC only exacerbate the uncertainties related to NorthWestern’s potential capital expenditures, regulatory relief requirements, and the timing of the company’s full earnings potential, in our opinion. Therefore, greater clarity of the company’s capital expenditure and rate case plans could still affect our earnings and equity assumptions materially over the next few years. Our estimates only reflect our understanding of currently anticipated and defined capital projects and rate filings. We are not ready to forecast the timing or magnitude of the Montana electric GRC we expect to be filed at some point. However, we do expect the MPSC to eventually approve new generation projects as they appear to advance state policy objectives. Given the considerably lower earned ROE, natural gas rate proceedings in Montana could be less difficult. However, the process may not always appear friendly as recent adverse MPSC orders have highlighted and could result in a more worrisome electric rate case, in our view.

We are reducing our 2017 recurring EPS estimate to $3.41 from $3.43 with quarterly estimates as shown on page 1. We generally expect operating cost controls initiated by management and warm Q317 temperatures to temper the Q217 shortfall. The reduced MPSC settlement agreement does not affect the 2017-2018 EPS figures materially. Our estimates largely reflect the Montana natural gas rate case settlement, a return to normal weather (with a better than normal Q117, below normal Q217, warmer than normal Q317, and near neutral Q417 temperatures compared with Q416), and revised O&M, property tax, and D&A expense assumptions. While 2016 had numerous visible earnings drivers, in the absence of new capital projects, acquisitions, or details of rate case filings, 2017 should be fairly simple, in our view. Essentially, we expect some operating cost pressures and de minimus equity dilution to be partially offset by better weather, load growth, improved gross margin, and the Montana natural gas rate increase.

Our 2017 estimates generally reflect:
- A return to more normal weather, a +$0.14 per share net benefit;
- An improvement in gross margin of $0.20, excluding weather;
- 1.0% retail energy load growth (+$0.09);
- and the Montana natural gas base rate increase (+$0.03, approximately 40% of the year).

We expect these positive catalysts to be partially offset by:
- O&M expense inflation of -$0.05 per share;
- DD&A expense inflation of -$0.12;
- property tax inflation (less tracker covered portion) of -$0.08;
- an increase in interest expense of -$0.00 which is moderated by the refinancing of a 6.0% issue that should largely offset higher debt balances;
- and -$0.00 equity dilution.

A higher effective tax rate of 9.0% is reflected in our estimates. Again, the outcome of natural gas resource acquisitions, new capital projects, and a potential material equity issuance could also influence 2017 results and beyond significantly. Our 2017 estimates reflect 48.6 million average diluted shares. While 2017 EPS should increase about 10% compared with 2016 due to a return to more normal weather, it is an unusual annual increase.

We are also reducing our 2018 recurring EPS estimate to $3.50 from $3.58 with quarterly estimates as shown on page 1. Our estimate represents roughly 2.6% annual EPS growth. The principal change to our outlook is the potential for equity dilution as discussed on the Q217 earnings call. We do expect credit rating downgrades. While we cannot account for how the tracker changes may affect NorthWestern’s cash...
flow yet, we are assuming $50 million of equity will be issued in late 2017/early 2018. The later the better to meet management’s 2017 guidance range. We estimate that $50 million is enough equity to provide about another 60 basis points of cushion to the FFO/debt ratio. Of course, greater than $50 million of new equity is always possible. Our estimates generally reflect a full-year Montana natural gas base rate increase (+$0.04), 1% retail energy load growth (+$0.09), an increase in gross margin (+$0.19), less net operating expense inflation of -$0.20 per share (largely O&M, DD&A, property taxes). Debt refinancing at lower cost and AFUDC for construction projects should also more than offset higher debt balances. A refinancing of $250 million, 6.34% debt should be particularly beneficial for the year. Our estimates reflect 49.6 million average diluted shares (-$0.07). A higher effective tax rate of 10.0% is also reflected in our estimates.

We are also reducing our 2019 recurring EPS estimate to $3.60 from $3.68, representing roughly a 2.9% increase in EPS compared with 2018. Our 2019 estimate largely reflects our assumptions for load growth, a small net Montana electric rate increase, and the likely 2018 equity dilution. More equity dilution than our $50 million assumption and strenuous power cost and/or property tax recovery mechanisms are risks to our outlook, in our view.

Other Recent Events

MPSC Settlement Reduction - On July 20, the Montana Public Service Commission (MPSC) approved a settlement agreement in the company’s natural gas rate case in docket D2016.9.68. The MPSC could not resist reducing further an already reduced settlement agreement by $0.6 million to +$5.1 million, +2.4% per annum. In doing so, the MPSC put out another of its self-serving press releases. The commission objected to some natural gas production benefits failing to live up to projections in 2010-2013.

In addition to another haircut coming from the MPSC at NorthWestern’s expense, the commission’s scrutiny of NorthWestern’s Cost of Service Gas (COSG) programs certainly will make incremental investments more difficult. More far reaching effects could be felt on the utility industry as a whole as this case will certainly draw the attention of other state regulators, making COSG investments in other states less likely as they point to the precedent of NorthWestern’s difficulty in meeting projected COSG benefits in their program.

MPSC Work Sessions - On June 22 and June 29, the Montana Public Service Commission (MPSC) held several work sessions addressing various NorthWestern related issues. While the MPSC addressed the passage of HB 193 in Montana which allows the commission to adjust NorthWestern’s power supply tracker, the tracker issue is now a relatively minor issue, in our view. Forget the fact that trackers are very common in the U.S. and help to reduce financing costs for consumers, the MPSC appears to abhor them nonetheless and any tracker changes are not likely to be beneficial to NorthWestern.

Of greater consequence was what followed. The MPSC reduced the terms on which Qualifying Facility (QF) generators can participate in the generation market. Most importantly, while the QF tariff rate was substantially reduced, limiting QF opportunities materially, the QF contract (PPA) term was also reduced to a maximum of 10 years with a rate adjustment after five years. Essentially, QFs now only have a five year contract to base financing on. While we are no fan of QFs, they have been an archaic concept that has inundated the western states with unacceptable consumer costs, these terms essentially kill off the QF market entirely, in our opinion. While that may have been the commission’s intention, what followed is unprecedented as far as we know.

NorthWestern suffered a new indignity as the MPSC voted to essentially hold the utility to the same QF standards for new generation resources. The commission put out one of its self-aggrandizing and unique to state commission press releases to signify the event. The commission bemoaned the risk of “forecast error”
in deciding to limit contract terms. Yes, forecast error does put consumers at some risk of a flawed forecast. Frankly, it is the commission’s role to determine the prudence of a power supply/market price forecast in determining if a new generation resource is prudent and in the interests of consumers. Saying “we accept the forecast for five years, then we will re-evaluate your investment” is not the regulatory compact as it exists in America today. A commission cannot adjust rates with perfect information in five years while the utility does not have that same opportunity. Someone has to make that determination before construction of new electric utility (or QF) assets, and that is the commission’s job. To later decide with actual information that an asset is imprudent after 100s of millions of dollars of investment has been made runs counter to the regulatory compact at its core. Frankly, utilities have generally done a good job of providing for utility resources on a timely basis. When they have not, they are not allowed to add additional resources until the actual consumer usage warrants a new investment. The necessity of this added condition on utilities in Montana appears unnecessary. The MPSC reiterated its intention to not guarantee fixed cost recovery of new generation resources beyond 10 years in its final order in the QF docket on July 21.

Natural Gas GRC Settlement - On June 12, NorthWestern announced a settlement agreement in its natural gas rate case. NorthWestern agreed to a $5.7 million, 2.9% increase in revenues. The settlement agreement is just over 50% of the initial $10.9 million revenue request. The settlement reflects a 9.55% ROE, 46.8% equity component as filed, and a 6.96% overall rate of return.

Q117 Conference Call - On the April 26 call, the company further reduced its CAPEX guidance through 2021 by about $80 million to reflect delays in new generation resource plans given the MPSC’s response to the company’s plan. NorthWestern CFO Brian Bird maintained the company’s expectations for attaining the lower-end of its 7%-10% annual total return target due to the lower capital expenditures and “regulatory headwinds” and delays regarding new generation investment proposals. Management previously noted that it increased the 2017 dividend growth to 5.0% partially to compensate for the lower prospective EPS growth.

Montana Gas Case - On April 7, the company filed its final rebuttal testimony in the Montana natural gas case. The company has reduced its rate request to +$9.4 million, +5.0% from the previous +$10.9 million, +8.0% amount. A decision is expected by mid-year.

Moody’s Downgrade - On March 10, Moody’s reduced the company’s credit rating one notch to A2 and maintained the negative outlook on NorthWestern.

Dividend Increase - On February 17, the company raised the common dividend 5.0% to $0.525, $2.10 from $0.50, $2.00. The increase represented a more aggressive increase compared to the 4.2% increase in 2015. As CFO Brian Bird noted on the Q416 earnings call, the more generous increase was related to lower near-term EPS growth expectations.

Investment Opinion

We reiterate our Hold investment rating and $64.00 target price on NorthWestern Corporation (NYSE: NWE) on July 27, 2017 at a price of $59.29. Our target price continue to reflect a material discount to peers of roughly 1.5x P/E turns our 2019 recurring EPS expectations that reflects the regulatory uncertainties of Montana. Currently, the stock is trading at nearly a 3.0x P/E discount to peers based on 2019 EPS that is beginning to appear somewhat attractive, in our view.

However, while the decline in NWE shares of late has led to a nearly 11.5% total return to our target price, we are not raising our investment rating at this time. The risks related to the potential for material equity dilution, further credit rating downgrades, additional adverse regulatory outcomes, and a potential for a
further degradation of NWE’s forward fundamental outlook given pending MPSC reviews of cost recovery mechanisms provide too much uncertainty at this point, in our opinion. Forget about the risks associated with a prospective Montana electric rate case, those are enough reason to give any investor heartburn. We could reconsider our rating with the stock somewhere in the $57.00-$58.00 range, providing a total return closer to 15%. Take note MPSC, the required rate of return on NWE equity is closer to 15.0% than 9.55%, write it down, we said it.

Our rating and target valuation reflects the significantly reduced growth outlook over the near-term and the unfavorable/contentious regulatory environment in Montana. The modest, below peer average intermediate-term growth outlook and a seemingly deteriorating Montana regulatory climate remain concerns for us. Nevertheless, NWE shares remain one of the less elevated valuations in the electric utility group. Still, the Montana situation is deserving of a material valuation discount. While the stock is trading at 16.5x our 2019 estimate, nearly 3.0x P/E turns cheaper than its electric peer group, the discount appears somewhat excessive, in our view. Still, we do not see enough upside potential in the stock to warrant adding NWE incrementally at this point, particularly in light of the highly volatile Montana regulatory environment.

Our target price reflects a P/E of 17.8x our 2019 EPS estimate, and roughly a 11.5% total return potential over the next 12 months, including the current indicated dividend yield of 3.54%. Our target valuation reflects a material discount to the average P/E for the stock over the past three years, but more comparable to average P/E relative to the past decade for NWE shares despite some higher comparable valuations, particularly in light of recent regulatory outcomes in Montana. Out target valuation reflects a discount to peers of about 1.5x based on 2019 earnings due to the Montana regulatory issues and lower comparable fundamental growth outlook for NorthWestern.

This year should be another positive EPS growth year (+10.0%) for the company despite unfavorable weather after an impressive decade of nearly 9.0% compounded EPS growth and a string of successful growth transactions. After the strong performance from 2015 results due to the Montana hydro asset acquisition, the acquisition of Beethoven wind farm, and the successful conclusion of the South Dakota electric base rate case, we expect another positive year in 2017 due to the reversal of the effects of very strong El Niño conditions on 2016. Cost control efforts should continue to be essential to future earnings growth.

We find the company enjoying many attractive characteristics at this time:

- **Valuation** - NWE share valuations have declined to near historical norms. While giving the stock a significant target P/E discount to the observed valuation of the previous three year average and a 1.5x discount to our target 2019 P/Es for our coverage universe (most of NorthWestern’s peers), the stock appears near fair value at close to its 10-year average P/E. The dividend yield of 3.54% is attractive relative to peer utility yields of closer to 3.0% in a yield-oriented market. Should regulatory relations improve or the growth outlook accelerate, the stock’s discount to peers would prove an attractive benefit. However, until then, NorthWestern’s low growth profile and regulatory issues is deserving of a lesser valuation.

- **Free Cash Flow** - NorthWestern is one of the rare utilities producing free cash flow that we expect to be in the $50-$75 million range annually for the next few years (based on the latest CAPEX budget). We love free cash flow generators.

- **Significant Growth Opportunities** - The company’s April 2016 Montana electricity supply resource procurement plan filing outlines a very attractive set of significant growth opportunities that we hope can successfully navigate the MPSC eventually. The plan also implies additional opportunities beyond the stated capacity goals and assumes what appears to be a very conservative load growth outlook.
**Exhibit 2: Our Valuation Worksheet**

<table>
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<tbody>
<tr>
<td><strong>EPS</strong></td>
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<td>$0.37</td>
<td>$1.30</td>
<td>$1.54</td>
<td>$1.44</td>
<td>$1.72</td>
<td>$1.68</td>
<td>$2.07</td>
<td>$2.47</td>
<td>$2.36</td>
<td>$2.56</td>
<td>$2.76</td>
<td>$2.98</td>
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<td><strong>Book Value</strong></td>
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<td>$33.22</td>
<td>$34.68</td>
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<td>$37.36</td>
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<tr>
<td><strong>Dividend</strong></td>
<td>$0.00</td>
<td>$0.00</td>
<td>$1.00</td>
<td>$1.24</td>
<td>$1.28</td>
<td>$1.32</td>
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<td>$1.48</td>
<td>$1.52</td>
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<td>$1.92</td>
<td>$2.00</td>
<td>$2.10</td>
<td>$2.20</td>
</tr>
<tr>
<td><strong>Payout</strong></td>
<td>0.0%</td>
<td>0.0%</td>
<td>77.0%</td>
<td>80.4%</td>
<td>89.2%</td>
<td>76.8%</td>
<td>79.7%</td>
<td>68.5%</td>
<td>58.4%</td>
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<td>64.3%</td>
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<td><strong>Oper. Cash Flow</strong></td>
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<td>$4.10</td>
<td>$4.58</td>
<td>$4.40</td>
<td>$5.45</td>
<td>$5.18</td>
<td>$3.22</td>
<td>$6.04</td>
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<tr>
<td><strong>Yield @ 3.25%</strong></td>
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<td>0.0%</td>
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<td>4.3%</td>
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<td>3.5%</td>
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<tr>
<td><strong>P/E @ 3.75%</strong></td>
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<td>$58.67</td>
<td>$61.33</td>
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<td></td>
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</tr>
<tr>
<td><strong>P/E-to-Book @ 1.6x</strong></td>
<td>0.0x</td>
<td>76.1x</td>
<td>23.9x</td>
<td>22.9x</td>
<td>20.6x</td>
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<td>16.9x</td>
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<td>18.3x</td>
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<td><strong>Price-to-Cash Flow @ 8.0x</strong></td>
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<td>1.4x</td>
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<td>1.7x</td>
<td>1.4x</td>
<td>1.1x</td>
<td>1.2x</td>
<td>1.3x</td>
<td>1.5x</td>
<td>1.4x</td>
<td>1.6x</td>
<td>1.8x</td>
<td>1.6x</td>
<td>1.6x</td>
<td>$57.37</td>
<td>$59.78</td>
</tr>
<tr>
<td><strong>EVEBITDA @ @ 12.0x</strong></td>
<td>12.4x</td>
<td>9.5x</td>
<td>8.0x</td>
<td>9.7x</td>
<td>8.8x</td>
<td>6.7x</td>
<td>6.0x</td>
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<td>9.0x</td>
<td>9.1x</td>
<td>9.5x</td>
<td>7.6x</td>
<td>9.5x</td>
<td>$59.95</td>
<td>$60.79</td>
<td>$62.23</td>
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<tr>
<td><strong>Average of Absolute Prices</strong></td>
<td>$0.08</td>
<td>$28.00</td>
<td>$31.07</td>
<td>$35.38</td>
<td>$29.50</td>
<td>$23.47</td>
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<td>$56.58</td>
<td>$54.25</td>
<td>$56.87</td>
<td>$60.12</td>
<td>$62.12</td>
</tr>
</tbody>
</table>

**Source:** Williams Capital estimates, NorthWestern

- **Stable Balance Sheet** - We expect a stable balance sheet squarely in the company’s 50%-55% debt target range for the foreseeable future without the need for material equity dilution in the absence of new electric generation needs or acquisitions.

- **Dividend Growth** - The company’s target dividend payout of 60%-70% suggests continued, if moderate dividend growth.

- **Strong Economy** - Economic growth in the company’s service areas is better than the overall U.S., leading to above average utility customer/energy demand growth for both electricity and natural gas utilities.

- **Gas Supply Acquisitions** - The company still has opportunities to acquire additional natural gas reserves in Montana and we expect new generation in Montana to fuel demand for natural gas over time.

- **Consistent Rate Base Growth** - Overall, capital expenditures well in excess of DD&A should yield additional significant rate base growth of $450-$600 million over the next five years.

- **Montana Electric Case** - The company also has opportunities for growth in a sooner-than-later necessary Montana electric base rate case due to a growing un-recovered rate base and a restructuring of the Dave Gates Generating Station. The company is currently earning below its allowed ROE.

- **ROE Stability** - Despite the drag of these last two issues, the company has been earning a respectable 9.0%-10.0% ROE for an extended period.

As Moody’s noted in reducing NorthWestern’s credit outlook to negative in 2016, the fundamental outlook for the company is significantly less clear after 2016 with few definitive fundamental drivers. The company is likely to require additional generation resources regularly over the next 20 years or so to address a widening gap between resources and peak demand loads. Yet, the opportunity remains unclear (particularly as it relates to the MPSC’s view).

**The MPSC is more than enough reason not to favor the stock.**

In the absence of new large investment/earnings opportunities over the near-term, in our opinion, the following uncertainties cloud the outlook for NWE shares:

- **Near-Term EPS Growth** - We expect only EPS growth of 3%-4% over the next few years. This level of growth is inferior to most of its peers and should weigh on the stock’s upside potential for now.

- **Rate Cases** - The growing gap between authorized and actual rate base in Montana will require a base rate case due to a growing un-recovered rate base and a restructuring of the Dave Gates Generating Station. The company is currently earning below its allowed ROE.

A modest growth outlook and regulatory issues weigh very heavily on the stock’s potential, in our view.
conservation/lost revenue recovery, etc. would be useful for the company, and are a beneficial staple in many other jurisdictions. Unfortunately, we do not expect any of these things from the MPSC.

- **Few Near-Term EPS Catalysts** - Until the realization of the Montana natural gas case growth, and a Montana electric base rate case filing, cost control efforts and load growth will dominate the company’s outlook and will put pressure on NorthWestern’s financial results after 2017, in our view.

- **Regulatory Environment** - The Montana Public Service Commission (MPSC) eliminated the Lost Revenue Adjustment Mechanism (LRAM) in 2015 in what appeared to us to be a punitive decision. Not only did the decision reduce annual revenues by about $7 million annually, in our opinion, it does not bode well for prospective Montana rate filings with this often capricious and mercurial commission. The Colstrip disallowance and legislative efforts to fight tracking mechanisms only reaffirmed that the MPSC can be an unreliable and shareholder unfriendly regulatory jurisdiction (again), in our view. Things have only gotten worse over time, in our opinion. The recent QF-related vote reducing the opportunities for new generation investment was only icing on what was already a bad cake.

- **Poorly Defined Growth** - While we were certainly excited by the company’s Montana electric generation resource needs, no Montana generation opportunity is yet to be approved, appears contentious, and remains uncertain in terms of amounts and timing. Certainly, much of the opportunity is outside of both our forecast period and valuation window.

- **Declining Tax Benefits** - As we approach later in the decade, declining tax benefits will eventually begin to put pressure on NorthWestern’s effective income tax rate, adding some additional pressure on the company’s financial results over time.

In our view, NorthWestern remains in a very good strategic position. The merits of NWE’s plain vanilla utility growth strategy appear only clearer in the current defensive market environment, in our opinion. The company will only require significant external equity if major growth projects beyond current CAPEX plans are pursued and refunding requirements are modest for a number of years. We expect rate base to grow modestly through 2021 due to less aggressive net rate base growth, natural gas production acquisition potential, distribution/transmission reliability capital spending, and with some further customer growth, in our view. The considerable decline in the stock since the 2016 peak also alleviated our concerns about previously excessive valuations, in our view. As we continue to monitor the company, additional insights into the company’s fundamental prospects and rate filing schedules/plans could prove material to our opinion over the next 12 months. However, generation resource investment delays are a disappointment. The regulatory environment for the company in Montana also scares us silly. We can see potential here, just not yet due to the regulatory risks currently present in Montana, despite the relative valuation gap evident in the stock.

**Valuation**

We see fair value for NWE shares of $64.00 being readily achievable over the next 12-months as the stock is valued more directly on 2019 earnings, dividend, and cash flow expectations, equity is issued, inevitable credit rating downgrades are completed, the base rate issues/outcomes/filings become clearer, regulatory risk is reduced, and new rates are implemented, in our view. We note that our target valuation is a composite of multiple techniques that does not rely solely on P/E to determine our target price.

We derive our 12-month valuation for the stock using multiple valuation methodologies, including a sum-of-the parts, price-to-earnings, price-to-book, dividend yield, price-to-cash flow, and Enterprise Value-to-EBITDA methodologies based on our 2019 fundamental estimates. We have valued NWE shares based largely on NWE’s average historic valuation metrics upon which the stock has traded over the past decade with further consideration of utility valuations since dividend tax cuts were enacted in May 2003, the divestiture of the majority of the more volatile non-regulated businesses and re-focus on pure utility operations, the prospective rate base and EPS growth, and the current defensive/yield oriented market.
In NWE’s case, we have valued the stock using a Dividend Yield range of 3.25%-3.75%, a Price-to-Book value of 1.5x-1.7x, a Price-to-Cash Flow value of 7.0x-9.0x, an EV/EBITDA value of 11.0x-13.0x and a P/E multiple of 17.0x-18.0x. Utilizing each of the aforementioned valuation methods, we derive a range of values of $61.00-$71.00 for the stock based on our 2019 fundamental estimates. Our target price is then effectively the average of theoretical stock price values derived from each of these valuation techniques. We note that our target price reflects a valuation comparable to the stock’s 10-year historic valuation metrics.

The stock is currently trading at 16.5x our 2019 recurring EPS estimate, at a 3.54% indicated dividend yield, and roughly 1.50x our estimated 2019 year-end book value (1.9x tangible book). In our opinion, the stock is currently trading at a material discount to peer electric utility group valuations that reflects an average P/E of nearly 19.0x-19.5x 2019 EPS and an average dividend yield of roughly 3.0% ex-Avista (NYSE: AVA, $52.61, Sell).

With the stock trading at only 16.5x our 2019 EPS expectations, the stock initially appears attractive relative to most utility peers. However, the company’s apparent growth profile pales by comparison to most peers. Our target valuation reflects a P/E valuation of 17.8x our 2019 recurring EPS estimates and a total return potential of about 11.5% over the next 12 months, including the current indicated dividend yield of 3.54%. In our view, our target valuation represents about a 1.5x discount to the peer group average valuation for electric utilities based on 2019 estimates. We note that the stock has generally traded for an average P/E of 16.7x, a median dividend yield of 4.1%, and a median price-to-book of about 1.5x, with a dividend payout of over 64% over the past decade. Over the past three years the valuations have been higher with a P/E averaging 18.3x, an average dividend yield of 3.5%, and an average price-to-book of 1.6x. However, the company’s growth outlook has weakened relative to the past three years, in our opinion.

In our view, NWE shares deserve a material discount to the combination utility group and its peers for a number of reasons. First, we are making educated assumptions about regulatory outcomes that are inherently risky and critical to NorthWestern’s growth and financial outlook. Second, the regulation of the MPSC is at best unfriendly to shareholders and adds to “forecast risk.” Finally, the growth is less attractive for NorthWestern for the next few years with limited insight into improvement in the regulatory climate in Montana, NorthWestern’s most critical jurisdiction. While the market remains defensive and focused on yield, we do not believe that a higher valuation is appropriate for NWE shares than we reflect in our target price.

Balance Sheet and Liquidity
NorthWestern’s balance sheet stands capitalized at about 45.8% equity, materially more highly levered than is typical for U.S. utilities today. Given rate cases over the near term that should raise annual earnings, and the company’s likely free cash flow production in most years based on current capital investment plans, we are comfortable with the company’s current temporary leverage. We expect a stable to modestly improving balance sheet due to growing operating cash flows. The company maintains approximately $113 million of consolidated ready cash/liquidity, including roughly $17 million of cash, through current credit facilities as of Q117 end, and has more than adequate access to the commercial paper and capital markets to fund prospective capital requirements, in our view. The company’s senior secured debt is rated A– at Standard & Poor’s, A2 at Moody’s, and A at Fitch. While S&P and Fitch have NorthWestern on Stable outlooks, Moody’s has had the company on negative watch since March 10.

Dividends
We believe that NorthWestern’s dividend is secure as we expect the 2017-2019 dividend payout to remain in the 60%-65% range for the next few years. Going forward, based on NorthWestern’s current CAPEX budget and prospective balance sheet improvement, we do not expect the company to require significant
external capital (certainly equity is very unlikely) over the next few years for other than debt refinancing. We do expect the significant improvement in 2017-2018 earnings and the stable utility source of those earnings to result in a moderate increase in the dividend (4%-5% annually).

As we expect continued earnings growth, and with the current indicated dividend payout (62.1% for 2017) well within the company’s targeted 60%-70% range, we expect the dividend to demonstrate sustainable growth. The dividend appears very secure, particularly given NorthWestern’s free cash flow generation and modest debt maturities through 2020, in our view. The stock is providing a current indicated dividend yield of 3.48% which we believe is attractive relative to the electric and natural gas utility groups.

NorthWestern has paid common dividends continuously since 2005. The company has increased the dividend every year since 2004. On February 17 the company raised the dividend 5.0% to $0.525, $2.10 per share from $0.50, $2.00 per share. In our view, management is dedicated to providing an attractive, competitive yield and a growing dividend. We expect the company to continue to increase the dividend annually at a 4.0%-5.0% rate during the current CAPEX program, consistent with the company’s current dividend policy/payout target and consistent with actual EPS growth that we expect. Some of the company’s debt covenants can restrict the payment of dividends under conditions that we do not expect.

The 3.54% current indicated dividend yield remains relatively attractive compared with fixed income alternatives and very attractive relative to comparable peer electric utility yields with an average yield of only about 3.2%. We note that the average yield on the stock over the last 10 years has been closer to 4.1%, but reflective of higher comparable interest rates and dividend yields, higher historical dividend payouts, a greater regulatory risk premium, and more variable earnings power and financial strength, in our view. Given our recurring EPS forecast, we believe that the company will be able to easily sustain the dividend payout that is now more in-line with the industry and that we expect to continue to decline over the next few years.

Regulatory Environment

NorthWestern Corporation, d/b/a NorthWestern Energy is regulated by the Montana Public Service Commission (MPSC), the Nebraska Public Service Commission (NPSC), and the South Dakota Public Utilities Commission (SDPUC). All three are elected commissions for six year terms. Both the Montana and Nebraska commissions consist of five members while the South Dakota commission consists of three. Over 80% of the company’s gross margin is derived from the Montana jurisdiction. The Montana commission has a nine month statutory review period and can allow interim rates, but rarely uses them. The South Dakota commission has a six month statutory review period and allows interim rates six months after filing. The Nebraska commission has a seven month statutory review period and allows interim rates 60 days after filing. The Montana legislature meets in alternate (odd) years. The company files an Electricity Supply Resource Procurement Plan (IRP) every two years (odd) that covers a 20 year forecast period.

Much like many elected commissions, the Montana Public Service Commission (MPSC) can certainly be as capricious and unfriendly to shareholders as the best of them, if not the worst in the U.S. The MPSC has a proven track record over the years. The mood of the MPSC changes as often as the commission elections that bring new commissioners to the bench. Just when we thought the MPSC had improved markedly in recent years, we are not sure where the MPSC sits today. The MPSC has now risen beyond the level of the New Mexico Public Regulation Commission (NMPRC), in our opinion.

Given the recent adverse rulings of the MPSC, we are very cautious about the regulatory environment in NorthWestern’s most critical state. We might normally wonder what management has done wrong to incite the commission. However, with Bob Rowe at the helm of the company, and given his experience as a commissioner in Montana, the situation suggests otherwise. As a result of the current state of regulatory
relations in Montana, we are more cautious about both growth at the company and the valuations we are currently willing to ascribe to the stock.

**Company Background**

NorthWestern Corporation, based in Sioux Falls, South Dakota is principally a combination electricity and natural gas utility that has a foundation dating back to 1913 in Montana. After failed non-regulated diversification efforts in the 1990s, the company filed for bankruptcy protection in 2003. Emerging from bankruptcy in 2004, the company has been virtually 100% utility focused since. The company has roughly 430,000 electric customers and 300,000 natural gas customers in Montana, South Dakota, and Nebraska. The company also serves Yellowstone National Park in Wyoming. While based in South Dakota, nearly 80% of the company’s customers and nearly 80% of the company’s gross margin comes from the Montana jurisdiction. Also, nearly 80% of the utility gross margin is derived from the electric utility. The company owns approximately 1,250 megawatts of electric generation.
20 Questions for Management

1) How do you interpret the MPSC’s current regulatory climate given the recent adverse regulatory decisions (LRAM, gas production, Colstrip disallowances, QF generation investment standard, the MPSC desire for a lower ROE apparently, tracker hatred, etc.)?

2) How do you react to the MPSC’s new generation investment cost recovery policy?

3) How do you expect to address revisions to your Montana generation resource plan?

4) How do you expect to address the credit rating downgrade/FFO-to-debt/equity dilution problem? How much, when?

5) Do the recent MPSC rulings and the current mood of the MPSC influence your investment thinking?

6) What can NorthWestern do to improve the Montana regulatory climate?

7) When do you expect to have greater insight into hydro expansion potential?

8) When do you expect to have more clarity on regional/state responses to the EPA’s plan and your capital plans?

9) How do you see Western EIM membership and NERC reserve margin requirements affecting your resource plan/company?

10) What are your thoughts on natural gas acquisitions in the current environment?

11) Other than your intentions for a Montana rate case filing, what else should we look for in your April Montana annual report filing?

12) What are your general thoughts on earned ROEs going forward?

13) How does the MPSC’s gas case settlement adjustment revise your natural gas acquisition strategy?

14) What is the latest on DGGS optimization?

15) Can we infer from your growth expectations that operating cost control efforts are a key element of your earnings growth plan for the near term?

16) When will you have more details on the MPSC tracker changes?

17) Can you elaborate on your South Dakota generation resource plan expectations?

18) Do you expect 5% to be a more constant dividend growth rate at this point or will annual increases vacillate over time?

19) Even Brian Bird doesn’t read these, we can stop at 19 this time.
**Valuation Methodology**

We see fair value for NWE shares of $64.00 being readily achievable over the next 12-months as the stock is valued more directly on 2019 earnings, dividend, and cash flow expectations, equity is issued, inevitable credit rating downgrades are completed, the base rate issues/outcomes/filings become clearer, regulatory risk is reduced, and new rates are implemented, in our view. We note that our target valuation is a composite of multiple techniques that does not rely solely on P/E to determine our target price.

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The stock is currently trading at 16.5x our 2019 recurring EPS estimate, at a 3.54% indicated dividend yield, and roughly 1.50x our estimated 2019 year-end book value (1.9x tangible book). In our opinion, the stock is currently trading at a material discount to peer electric utility group valuations that reflects an average P/E of nearly 19.0x-19.5x 2019 EPS and an average dividend yield of roughly 3.0% ex-Avista (NYSE: AVA, $52.61, Sell).

With the stock trading at only 16.5x our 2019 EPS expectations, the stock initially appears attractive relative to most utility peers. However, the company’s apparent growth profile pales by comparison to most peers. Our target valuation reflects a P/E valuation of 17.8x our 2019 recurring EPS estimates and a total return potential of about 11.5% over the next 12 months, including the current indicated dividend yield of 3.54%. In our view, our target valuation represents about a 1.5x discount to the peer group average valuation for electric utilities based on 2019 estimates. We note that the stock has generally traded for an average P/E of 16.7x, a median dividend yield of 4.1%, and a median price-to-book of about 1.5x, with a dividend payout of over 64% over the past decade. Over the past three years the valuations have been higher with a P/E averaging 18.3x, an average dividend yield of 3.5%, and an average price-to-book of 1.6x. However, the company’s growth outlook has weakened relative to the past three years, in our opinion.

In our view, NWE shares deserve a material discount to the combination utility group and its peers for a number of reasons. First, we are making educated assumptions about regulatory outcomes that are inherently risky and critical to NorthWestern’s growth and financial outlook. Second, the regulation of the MPSC is at best unfriendly to shareholders and adds to “forecast risk.” Finally, the growth is less attractive for NorthWestern for the next few years with limited insight into improvement in the regulatory climate in Montana, NorthWestern’s most critical jurisdiction. While the market remains defensive and focused on yield, we do not believe that a higher valuation is appropriate for NWE shares than we reflect in our target price.

**Risk**

In our view, NorthWestern Corporation common shares represent the level of risk that we believe is inherent in an average publicly traded stock/company. Since the Montana PSC authorized Colstrip Unit 4 in regulated rate base, much of the commodity volatility/uncertainty in the company’s earnings profile has been reduced. However, the company remains materially short generation (-28% reserve margin). In our view, NorthWestern’s risk profile is significantly elevated relative to the average combination electric and natural gas utility due to its small size, the considerable capital growth program the company is undertaking, and the greater regulatory risk associated with the Montana PSC (currently elevated). Nevertheless, the company is entirely composed of traditional regulated utilities, which is an important factor in our risk assessment. We do not foresee any material financial risks at this time. The company is well capitalized and the company’s liquidity as represented by its cash flow and fixed charge coverage is very good, in our view. As the company completes its capital programs and potential prospective Montana rate cases, we believe NorthWestern’s risk profile should actually become more aligned with a lower risk profile in time, assuming less adverse future decisions from the MPSC.

However, significant delays in filing a Montana electric rate case could begin to affect the company’s financial results starting in 2017 as significant capital investments could go without requisite revenue recovery. Difficulty in completing and/or financing the company’s growth projects could also materially affect the company’s growth profile, earnings and cash flow results, and investor interest in the stock. The regulatory response to the company’s investment plans could also affect the timing and ultimate impact of potential investments on earnings and cash flow. The Montana regulatory environment is always a significant risk. However, we believe the company will continue to improve its relationship with Montana regulators and we believe that there is local support for much of the company’s infrastructure investment plans in the long term. A significant rise in interest rates or dividend tax rates could also put significant pressure on utility operating costs and utility equity valuations. At this point, we are more worried about macroeconomic issues affecting the stock than company fundamentals other than the Montana regulatory environment. However, the Montana regulatory environment requires constant monitoring given recent adverse decisions and policies.
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I, Christopher R. Ellinghaus, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject companies and their securities. I further certify that no part of my compensation was, is, or will be directly, or indirectly, related to the specific recommendations or views contained in this research report.

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WILLIAMS CAPITAL EQUITY RESEARCH RATINGS KEY

BUY: In the analyst’s opinion, the stock will outperform the S&P 500 on a total return basis over the next 12 months.
HOLD: In the analyst’s opinion, the stock will perform in line with the S&P 500 on a total return basis over the next 12 months.
SELL: In the analyst’s opinion, the stock will underperform the S&P 500 on a total return basis over the next 12 months.

DISTRIBUTION OF EQUITY RESEARCH RATINGS AS OF: JULY 26, 2017

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