Eversource Energy

More questions than answers after 4Q call and offshore wind transactions

Reiterate Rating: UNDERPERFORM | PO: 50.00 USD | Price: 57.06 USD

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Equity

Paul Zimbardo
Research Analyst
BofAS
paul.zimbardo@bofa.com

Julien Dumoulin-Smith
Research Analyst
BofAS
julien.dumoulin-smith@bofa.com

Still see challenges to the reaffirmed 5-7% EPS growth

We reiterate our Underperform on Northeast regulated utility and offshore wind developer Eversource Energy (ES) after the 4Q23 earnings update and offshore wind transaction update. ES outperformed utility peers +4-5% after the update which we attribute to the company maintaining its 5-7% EPS growth rate ($4.34 2023 base) which is above BofA/Consensus and a headline of offshore wind proceeds. We do not forecast that ES can achieve the 5% EPS growth rate on a sustained basis due to required balance sheet repair. With at least 200-300bp annualized equity dilution (potentially 5%) plus growing parent costs (interest expense and income taxes), our model supports de minimis EPS growth.

Significant offshore wind exposure a cautious surprise

The most cautious update in the update is that ES is effectively retaining full economic exposure to Revolution Wind construction, financing, taxes, etc. by guaranteeing a 13% internal rate of return for the buyer GIP. ES stated that it has $255Mn Revolution Wind and $300Mn South Fork fair value versus the $1.1Bn guided proceeds. Per the 10K, we expect that ES will need to finance capital contributions through mid-2024 which reduces net proceeds; ES did not quantify this spending but stated it is not significant.

2023 EPS +2% ex parent income. 2024 + tax drivers

The biggest earnings driver in 2023 was parent and other, +$0.15 with +$0.03 absolute adjusted EPS from the cost center. This was despite approximately $100Mn higher other income expense (~$0.25). Excluding parent, ES grew adjusted EPS +2%. ES initiated $4.50-$4.67 FY24 adj EPS guidance vs $4.37 BofA and $4.49 Consensus. FY24 adj EPS guidance includes an increase in tax benefits YoY. Management stated that the 2023 effective tax rate was in the high teens and it expects 18-20% in 2024. Per the 10K, the consolidated 2023 effective tax rate was negative -58% with 22-25% utility effective tax rates. We estimate that tax benefits are +$0.25 to +$0.30 benefit 2024 vs 2022.

Balance sheet remains critical & improvement is not clear

ES did not quantify its 2023 FFO / debt but indicated low double digits which we estimate is likely 10-11%. FY23 cash flow from operations was $1.65Bn, down sharply from $2.4Bn in 2023. With $26Bn+ debt at 12/31/23, credit metrics appear even lower than we forecasted. Favorably adjusting for $800Mn amortization, operating cash flows were effectively flat. Management guided to 14-15% by 2025, a significant improvement assuming one-time benefits from ~$500Mn tax equity proceeds and seemingly the $800Mn amortization reversal. We model FFO / debt ~13% with $3.3Bn equity issuance. Consistent with investor expectations, ES stated that it is exploring the sale of its Connecticut water pipeline company Aquarion in addition to "up to" $1.8Bn equity 2024-2028 ($1.3Bn ATM+ ~$0.1bn/yr in DRIP). Sunrise wind sale would reduce this figure. Aquarion could be upside but we remain skeptical of material accretion given the challenging Connecticut regulatory backdrop. ES acquired for $1.7Bn EV ($900Mn cash and $800Mn debt) in June 2017 when long-term Treasuries were 2.9% and Connecticut was a better regulatory jurisdiction. We value Aquarion at $1.7Bn EV again today: 1.3x YE23 rate base, 22x 2023 P/E, and 11x 2026 P/E.

Stock Data

Price	57.06 USD
Price Objective	50.00 USD
Date Established	16-Oct-2023
Investment Opinion	B-3-7
52-Week Range	52.03 USD - 81.36 USD
Mrkt Val (mn) / Shares Out (mn)	19,962 USD / 349.9
Free Float	99.1%
Average Daily Value (mn)	194.13 USD
BofA Ticker / Exchange	ES / NYS
Bloomberg / Reuters	ES US / ES.N
ROE (2023E)	9.7%
Net Dbt to Eqty (Dec-2022A)	140.8%
ESGMeter™	High

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GIP: Global Infrastructure Partners
FFO: Funds from operations
CWIP: Construction work in progress

Refer to important disclosures on page 4 to 6. Analyst Certification on page 3. Price Objective Basis/Risk on page 3.

High offshore wind risks remains

Eversource stated that its $1.2Bn impairment of Sunrise Wind incorporated termination costs and a scenario of not being successful in the rebid with neither sales proceeds nor investment tax credit value. The 10K states that if Sunrise does not win the New York solicitation, it could abandon the project and there would be cancellation/abandonment costs above the those assumed in the impairment evaluations. Eversource warns that it could face credit rating downgrades and liquidity issues if the value of its offshore wind projects are not realized. Orsted disclosed a 75% probability of winning the Sunrise rebid in its financial update and it is unanimous from our investor conversations that the project is successful in the New York solicitation rebid. Per Orsted, there appears to be ~$900Mn of cancellation/abandonment costs for Eversource's share of the project if unsuccessful.

Eversource's 10K further indicates that there is uncertainty regarding the investment tax credit (ITC) incentive qualification for Revolution Wind and there could be material future impairments. ES will share 50% in the first ~$240Mn incremental capex overruns with Eversource responsible for 100% for the next further potential overruns. The 13% IRR true-up for all factors appears to leave Eversource shareholders fully exposed to offshore wind construction risk for the next year-plus. There is downside to ES' proceeds if it is not eligible for the +10pp energy community investment tax credit bonus.

Capex increases but rate base updates lag

Eversource did not provide YE23 rate base information but YE22 rate base lagged our expectations. YE22 rate base is $25.4Bn plus ~$1.3Bn construction work in process. This compares with $24.4Bn YE21 plus ~$2Bn construction work in process. Rate base increased only +4% in 2022 and rate base plus CWIP only grew +1%. A +$1,000Mn rate base and +$300Mn rate base plus CWIP increase YoY for 2022 despite $3.8Bn capex and $1.2Bn depreciation is notably light.

Exhibit 1: Eversource Year-End Rate Base and Construction Work in Progress (CWIP) Guidance
ES 2022 rate base guidance disappointed

Eversource Rate Base Guidance	YE21	YE22	YE27	YE28	'21-'27	'22-'28
Rate Base	24,400	25,400	37,700	39,600	7.5%	7.7%
CWIP	2,000	1,300	3,000	2,600	7.0%	12.2%
Total Rate Base + CWIP	26,400	26,700	40,700	42,200	7.5%	7.9%
YoY		1.1%		3.7%		

Source: Company Filings

BofA GLOBAL RESEARCH

Earnings mix in sharp focus

Eversource still forecasts significant pension and related income in 2024 although a -$15Mn decline YoY. We estimate $0.13 net/untracked pension income (3% of EPS), one of the larger contributions in our coverage universe. This type of pension income has been under more focus with peer FirstEnergy (FE) describing pension income as 'lower quality earnings.

Price objective basis & risk

Eversource Energy (ES)

Our sum of the parts based price objective of $50 uses P/E multiples on 2026E earnings. The valuation is based on a 2025 sum of the parts analysis. We apply the 2026 average peer P/Es of 13.1x electric, 13.3x natural gas, and 17.5x water. For Connecticut electric & gas utilities, we value at -20% discount (-2.8x) to reflect historical challenges and prospective earnings risks. Connecticut water is valued in-line with natural gas. The other utilities are valued at a -15% discount (-2.1x) for below-average consolidated growth and weaker balance sheet metrics. Parent net loss per share is valued at an -1x discount to the electric utility average.

Upside and downside risks to our Price Objective are 1) regulatory/political/legislative changes, 2) capital expenditures forecasts, 3) ability to earn the regulatory allowed ROE, 4) offshore wind review, 5) natural disasters & storms, 6) operational performance and gas incidents, 7) integration of historical and prospective M&A, 8) pension plan performance, and 9) equity issuances.

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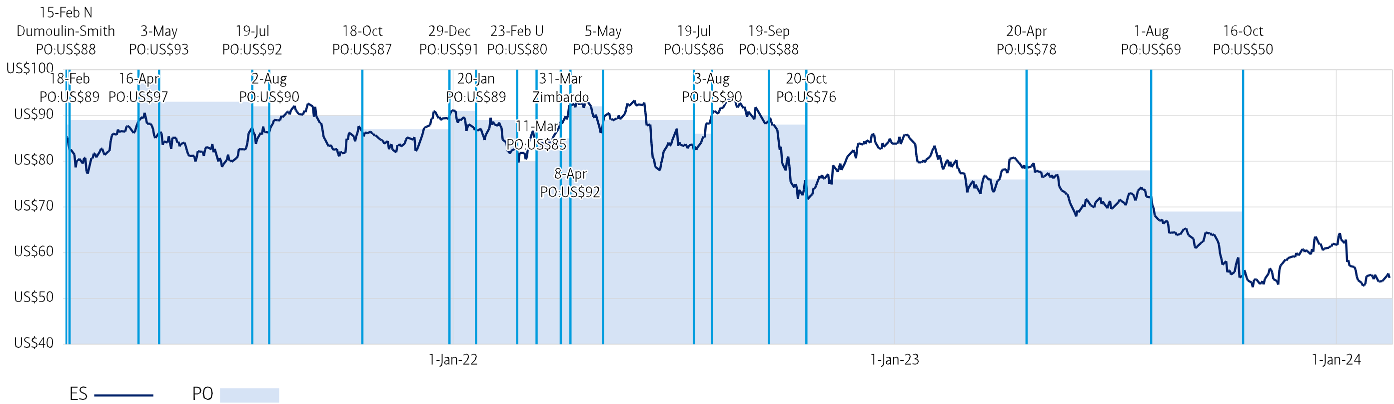
Eversource Energy (ES) Price Chart



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Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	72	46.45%	Buy	52	72.22%
Hold	45	29.03%	Hold	32	71.11%
Sell	38	24.52%	Sell	21	55.26%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

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Sell	807	22.84%	Sell	383	47.46%

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