

US Utilities & Clean Tech

PowerPoints: XEL Growth, PNW Arizona, PCG Safety, and Offshore Wind Latest

Industry Overview

XEL: Growth expected above top end of 5-7% range

Xcel Energy's (XEL) highly anticipated 4Q23 update led to an extension of the long-term EPS growth profile at the top-end of the 5-7% growth target. We had anticipated a stronger signal with a formal increase to 6-8%; however, nearly all our investor conversations focused on the high-end of 5-7%. Ultimately we believe this is a degree of semantics with XEL likely growing 7-8% when factoring in positive compounding with the company rebasing off actuals. The earnings call commentary was constructive as management pointed to EPS growth above the top end of its 5-7% range beginning in 2025 as the new capital spend begins to flow through rate base. Premium peer CMS Energy (CMS) is one of the only other companies that rebases off actual results versus the prior year's midpoint, a positive trait. Taken together the commentary suggests that coming acceleration in spend and earnings growth will be sustained for some time (Texas capex is yet more upside not yet in the plan) but that eventually growth should revert to historical levels. We remain confident in our earnings estimates which are consistent with the 'above the top end' commentary as the bulk of Colorado generation and transmission spend is invested. Note also that XEL's strong financial performance has been cited in recent regulatory proceedings by stakeholders and the EPS growth sends a signal to a variety of stakeholders. *We maintain Buy on XEL as one of the increasingly few premium regulated utilities which still has future capex upside from renewable generation opportunities in Texas and elsewhere.*

PNW: Proposed order supports SRB, higher ROE

The Arizona Corporation Commission administrative law judge (ALJ) in the Arizona Public Service (APS, Pinnacle West [PNW] subsidiary) rate case issued a recommended opinion and order (ROO) on January 25th, in line with the expected timeline. Key components of the recommendation include a 9.55% ROE (up from 8.7% in the previous case which was adjusted up to 8.9% following legal appeal), 0.25% return on fair value increment (FVI), and use of APS' actual equity layer which is consistent with historical practice. The ROO supports APS' proposed system reliability benefit (SRB), a modified version of the generation rider originally proposed – this is also not surprising given the outcomes of earlier rate cases for Fortis (FTS) in Arizona. The ROO contains substantial modifications to the original proposal including a cap on deferrals of any amount exceeding the 3% year-on-year cap, an earnings threshold test, one filing within a 12-month period, and prudence review by the commission, among other modifications. One negative recommendation is disallowance of pension expense 'normalization' which would have averaged 2022 and 2023 pension expense, resulting in a ~\$26m reduction. All in the ROO proposes a base rate increase of +\$577m or 15.9% as compared to \$690m requested by the company – at over 80% of the requested amount this represents one of the more constructive rate cases across our coverage in recent memory. We maintain Neutral on shares of PNW which have a balanced risk/reward and we look for a long-term earnings growth refresh with 4Q23 earnings.

29 January 2024

Equity
United States
Utilities & Clean Tech

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ROO: Recommended opinion and order
FVI: Fair value increment
SRB: system reliability benefit
PG&E: Pacific Gas & Electric
OEIS: Office of Energy Infrastructure Safety
MWh: Megawatt hour

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Timestamp: 29 January 2024 10:38AM EST

XL: Further Thoughts

We see the backdrop on deciding not to move higher with its 5-7% EPS CAGR as respecting the regulatory backdrop more than any specific concern on the outlook. We appreciate the ongoing scrutiny applied in Colorado and saw the pullback on the margin in timing/size of proposal as in part reflecting some rate sensitivity. We appreciate the clear upward latitude in the program with its base ratebase growth enabling the top-end of EPS estimates already, prior to reflecting either the 'core' upside of \$5 bn or the 'upside to the upside' in the full SPS expansion of \$5Bn+ (seemingly *another* \$5 bn+ of opportunity). On balance, we see latitude towards a healthy 7% figure with aspirations towards 8% EPS clearly in view.

On the regulatory front, we perceive more muted near-term risks. Natural gas in Colorado could prove an issue anew with the latest rate case in front of us, but we perceive much of the issues tied to bills to be legacy. Watch for some potential evolution on gas cost recovery. Much of the regulatory focus likely remains on just procurement, with SPS likely to garner a growing debate between NM/TX on the composition of the 5-10GW buildout and the amount that will be 'ownable' by SPS (via procurement; again, recall AEP SWEPCo's own recent challenges, although we think lessons have been learned there from all already).

Equity is the near-term focus: timing/size of equity in the near-term (beyond likely ~\$2.5 Bn of ATM thru the plan) as well prospects for upside.

PCG: Annual safety certificate granted without fuss

On January 22nd, the California Office of Energy Infrastructure Safety (OEIS) issued Pacific Gas & Electric (PG&E [PCG subsidiary]) safety certificate for the next twelve months. The recommendations are not onerous and management appears to have agreed to implement them all. Historically the granting of the safety certificate was an area of uncertainty and investor focus but this has fortunately become more of a routine exercise for PG&E and its California peer utilities. *We maintain Buy on shares of PCG which remain a top utility pick, trading at an overly large discount versus peers.*

Offshore Wind: New York and New Jersey latest

New York bids roll in as partnerships form with Eversource a prime example

The New York State Research and Development Authority (NYSERDA) reported that it received six bids from three offshore wind projects in the fourth competitive solicitation (NY4). Bidders include Community Offshore Wind 2, Empire Wind 1, and Sunrise Wind – we detail the latest developers for each.

Eversource Energy (ES) announced that it is conditionally selling its 50% stake the Sunrise Wind offshore wind project back to its joint venture partner Orsted at an undisclosed price, assuming a successful award from New York. We assume immaterial value and currently embed ~\$500Mn proceeds for all of ES' offshore wind portfolio. The transaction on January 24th came the day before the deadline to rebid into New York offshore wind solicitation on January 25th. If Eversource/Orsted are successful in winning a new contract from New York, Orsted will purchase Sunrise Wind and Eversource with 50% payment upon close and 50% upon completion of onshore construction and other milestones. If Sunrise Wind does not receive a new contract in the solicitation, the 50%/50% joint venture would remain.

Orsted also announced that it will "reposition" its ~1GW Maryland Skipjack wind project and has withdrawn from its Maryland Public Service Commission (PSC) contracts. Eversource's projects continue to be delayed with the small Southfork Wind commercial operations now "in the weeks ahead" and Sunrise in 2026 versus late 2025 previously. We plan to watch the timeline on Sunrise closely as final Federal approval is pending with Eversource/Orsted expecting mid-2024.

Other parties realign their partnerships like Eversource/Orsted

Equinor (EQNR) announced that it has a swap transaction with bp to take 100% ownership of Empire Offshore Wind and bp will take Beacon Wind and the related energy assets in a cash neutral transaction. Equinor expects to lose ~\$200Mn USD, assuming it wins a new contract from New York. Equinor bid into the New York solicitation with Empire Wind 1 and Empire Wind 2 will participate in future solicitations.

Equinor guided to a real base project return in the lower-end of 4-8% range.

RWE and National Grid (NG) bid their 1.3GW Community Wind into the NY RFP, following winning 1.3GW in the last NY offshore wind (NY3).

ES was a top performing regulated utility on January 24th before the after-hours 8K and continued to rally in the following days. From our conversations, investors expect the Sunrise rebid to be successful with no risk sharing for ES on Sunrise Wind as well as a sale of Revolution/South Fork wind in the upcoming days before 4Q23 earnings. Most investors we speak to are increasingly positive on ES with what we believe is a challenged view that simply exiting offshore wind cures the company's woes. The core challenge ES has been facing for years is one of the worst credit metrics in the sector (10-12% funds from operations to debt historically) and a challenging Connecticut regulatory backdrop that manifests in below average EPS growth. We model approximately flat earnings 2023-2025 with below average earnings growth prospectively. *We maintain Underperform on shares of ES which are relatively expensive and have the large equity dilution risk.*

New Jersey prices at \$119/MWh future dollars or \$89/MWh 2023 dollars

The New Jersey Board of Public Utilities (BPU) awarded twenty year offshore wind contracts to Attentive Energy Two (1.3GW TotalEnergies 70%/Corio 30% joint venture for 2031 commercial operations) and Leading Light Wind (2.4GW Invenergy and energyRe joint venture for 2032 commercial operations). Attentive Energy One separately won 1.4GW New York round three solicitation.

Leading Light Wind has a 20Yr contract with \$112.50/MWh first-year nominal contract price with a +2.5% annual inflation adjustment.

Attentive Energy Two, has a 20Yr contract with \$131/MWh first-year nominal contract with +3% annual inflation. Total stated that the bid assumes a 30% Inflation Reduction Act (IRA) investment tax credit (ITC). There is also a one-time inflation adjustment mechanism that can reflect capital cost changes before a final investment decision (FID).

Bloomberg New Energy Finance (BNEF) estimated that the first year capacity-weighted average nominal tariff is \$119.13/MWh and is \$89.12/MWh in \$2023 dollars. This is +23% higher than the \$72/MWh in the NJ round two solicitation.

We will be closely watching future offshore wind bids to see how pricing evolves. There was a notable increase in comparable pricing versus the last NJ solicitation but there was not the significant +50% increase that some investors had contemplated with strong competitive forces at play. For example, in the pending New York auction, Equinor's 4-6% real base project return target disclosed will likely be a factor in how other parties bid.

Exhibit 1: Primary stocks mentioned in this report

Prices and ratings for primary stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
XEL	XEL US	Xcel Energy	US\$ 60.91	B-1-7
PNW	PNW US	Pinnacle West Capital	US\$ 71.37	B-2-7
PCG	PCG US	PG&E Corp.	US\$ 16.99	B-1-7
ES	ES US	Eversource Energy	US\$ 55.12	B-3-7

Source: BofA Global Research

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Price objective basis & risk

Eversource Energy (ES)

Our sum of the parts based price objective of \$50 uses P/E multiples on 2025E earnings. The valuation is based on a 2025 sum of the parts analysis. We apply the 2025 average peer P/Es of 13.5x electric, 13.5x natural gas, and 20.0x 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.

PG&E Corporation (PCG)

Our PO of \$19 reflects an in-line P/E versus the respective electric (16.1x) and gas (16.0x) peer P/E groups with both grossed-up by 5% to reflect capital appreciation across the sector) based on 2025E. The acute wildfire risk is incorporated separately via a scenario probability weighted at 100% assuming PCG hits the cap in 3-year increments. Lastly, we net out 50% weighting of HoldCo debt and add back 50% weighting of interest expense to derive our Price Objective.

Risks to achievement to estimates and Price Objective are: 1) Wildfire and other natural disasters/catastrophic events, 2) regulatory outcomes, 3) interest rates, 4) equity needs, 5) earned returns and operating costs, 6) Fire Victim Trust monetizations, 7) ability to deploy capital, 8) asset sales, 9) management changes, and 10) environmental, social, & governance [ESG] profile.

Pinnacle West (PNW)

Our price objective of \$71 is based on a peer utility P/E multiple of 13.8x, grossed up for a year by 5% to reflect capital appreciation across the sector.

For Arizona Corporation Commission (ACC) regulated assets we apply a -1x discount to reflect the relative quality of the jurisdiction and ongoing earned ROE lag.

For Federal Energy Regulatory Commission (FERC) regulated assets we apply a +3x premium to reflect a premium ROE and rider recovery of invested capital.

Upside and downside risks to the Price Objective are changes in 1) regulatory, political, and legislative relationships/outcomes, 2) load growth in territory versus expectations, 3) riders and capital trackers implementation 4) weather, nuclear, and natural disasters, 5) interest rates, 6) pension liabilities and asset returns, 7) equity needs relative to forecasts, 8) capital expenditures, and 9) ability to control costs to earn a return on equity.

Xcel Energy Inc (XEL)

Our PO is \$69. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we

divide the segments by subsidiary.

We use 2026E forward P/E multiple of 13.8x to derive a value for the different business segments, including the parent segment. Electric peer P/E multiple is grossed up for a year to reflect capital appreciation across the sector. We make an additional adjustment to reflect the difference in interest rate forecasts between BofA and Street as well as historical valuation sensitivity to rates.

We apply a 2x premium to XEL subsidiaries in MN and 3x for CO, 3x for NM/TX, and 3x for WI as both utilities present solid or improving regulatory treatment with tangible investment upside. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Risks to achievement of the price objective are interest rate changes, regulatory risk, such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, inability to deploy capital at guided levels, adverse legislation, execution delays, and weather/natural disasters

Analyst Certification

We, Julien Dumoulin-Smith and Paul Zimbardo, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North America - Utilities and Alt Energy Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	Array Technologies	ARRY	ARRY US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Enlight Renewable Energy Ltd	ENLT	ENLT US	Julien Dumoulin-Smith
	Enlight Renewable Energy Ltd	XENLF	ENLT IT	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Paul Zimbardo
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	Fluence Energy	FLNC	FLNC US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	MDU Resources Group, Inc.	MDU	MDU US	Julien Dumoulin-Smith
	Nextacker Inc	NXT	NXT US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NorthWestern Energy Group	NWE	NWE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Paul Zimbardo
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra	SRE	SRE US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	TPI Composites	TPIC	TPIC US	Julien Dumoulin-Smith
	Vistra Corp	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Paul Zimbardo
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Paul Zimbardo
	AltaGas	YALA	ALA CN	Cameron Lochridge
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Ameresco	AMRC	AMRC US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	ChargePoint Holdings	CHPT	CHPT US	Cameron Lochridge
	Constellation Energy Corp	CEG	CEG US	Paul Zimbardo
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Paul Zimbardo
	Generac Holdings Inc.	GNRC	GNRC US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Paul Zimbardo
	Maxon Solar Technologies	MAXN	MAXN US	Julien Dumoulin-Smith
	New Fortress Energy	NFE	NFE US	Cameron Lochridge
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Southwest Gas Holdings	SWX	SWX US	Julien Dumoulin-Smith
	TransAlta Corp	TAC	TAC US	Julien Dumoulin-Smith
	TransAlta Corporation	YTA	TA CN	Julien Dumoulin-Smith

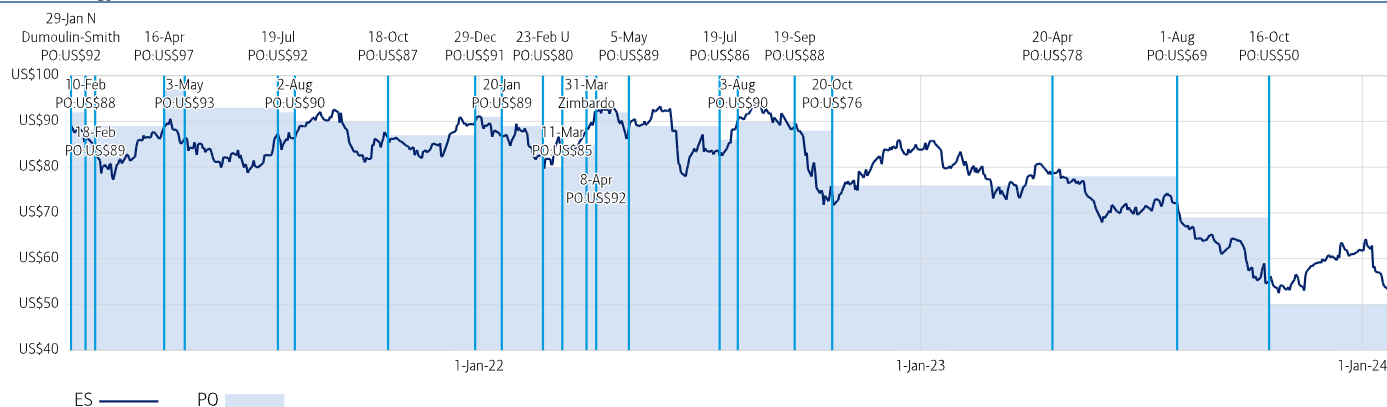
North America - Utilities and Alt Energy Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
UNDERPERFORM	Allete Inc	ALE	ALE US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Paul Zimbardo
	Avista	AVA	AVA US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Paul Zimbardo
	Edison International	EIX	EIX US	Paul Zimbardo
	Enphase Energy	ENPH	ENPH US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Paul Zimbardo
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	FREYR Battery	FREY	FREY US	Julien Dumoulin-Smith
	FTC Solar	FTCI	FTCI US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Julien Dumoulin-Smith
	SolarEdge Technologies	SEDG	SEDG US	Julien Dumoulin-Smith
	Spire	SR	SR US	Julien Dumoulin-Smith
	Stem, Inc.	STEM	STEM US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

Disclosures

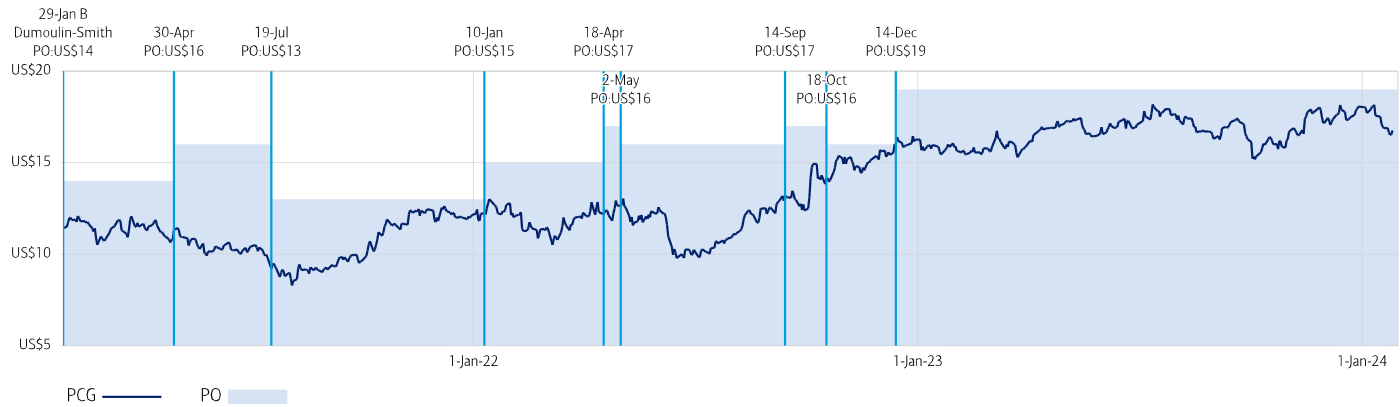
Important Disclosures

Eversource Energy (ES) Price Chart



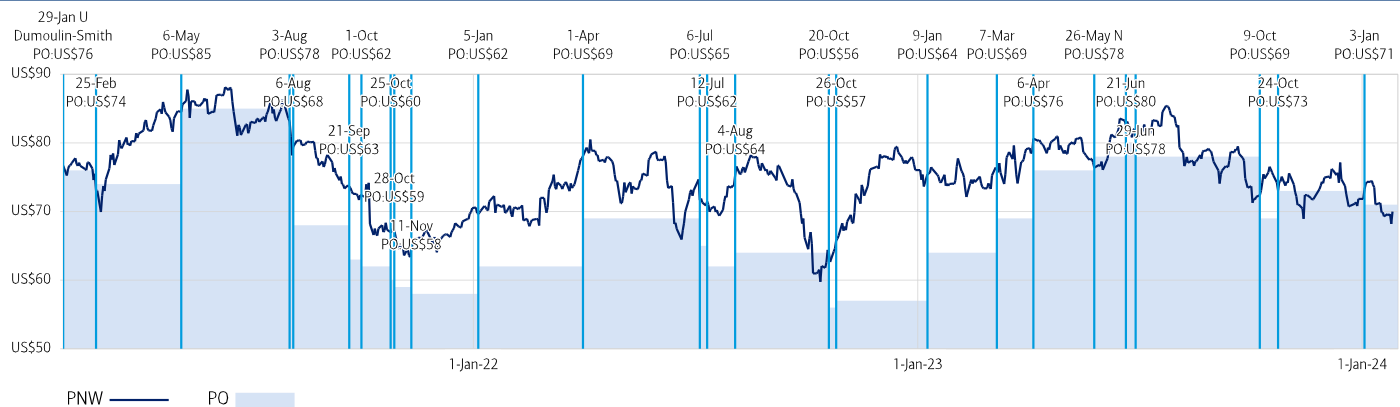
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

PG&E Corp. (PCG) Price Chart

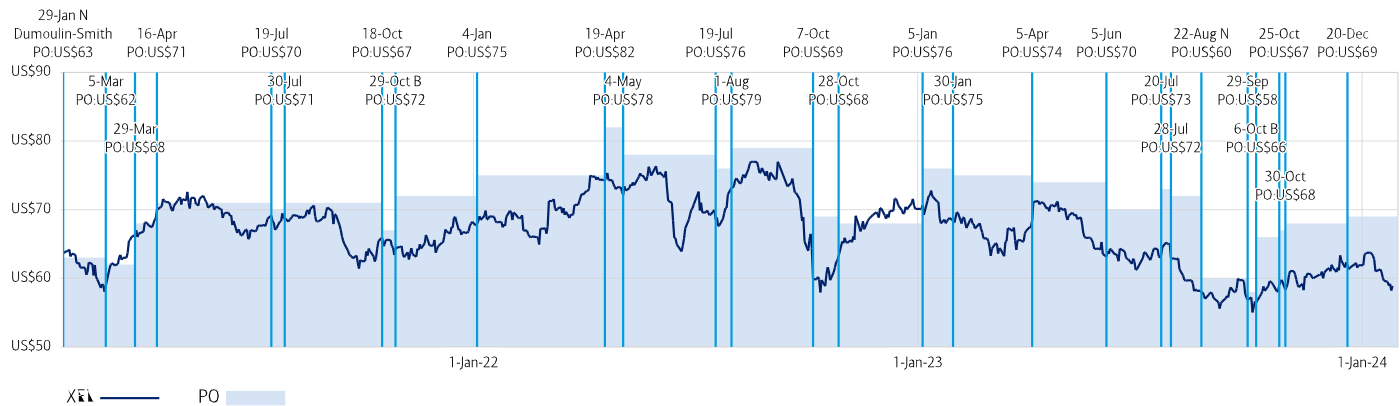
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Pinnacle West Cap (PNW) Price Chart

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Xcel Energy (XEL) Price Chart

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

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

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)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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