

Q3 2018 Earnings Call

Company Participants

- Lynn Good, Chairman, President, Chief Executive Officer
- Michael Callahan, Vice President, Investor Relations
- Steven Young, Vice President, Chief Financial Officer

Other Participants

- Ali Agha, Analyst, SunTrust
- Greg Gordon, Analyst, Evercore ISI
- Jonathan Arnold, Analyst, Deutsche Bank
- Michael Lapedes, Analyst, Goldman Sachs
- Michael Weinstein, Analyst, Credit Suisse
- Praful Mehta, Analyst, Citi
- Shahriar Pourreza, Analyst, Guggenheim Partners
- Stephen Byrd, Analyst, Morgan Stanley
- Steve Fleishman, Analyst, Wolfe Research
- Unidentified Participant

Presentation

Operator

Good day and welcome to the Duke Energy Third Quarter Earnings Call. Today's conference is being recorded. At this time, I'd like to turn the conference over to Mr. Mike Callahan, Vice President of Investor Relations. Please go ahead, sir.

Michael Callahan {BIO 19728882 <GO>}

Thank you, Cody. Good morning, everyone, and thank you for joining Duke Energy's third quarter 2018 earnings review and business update. Leading our call today is Lynn Good, Chairman, President and CEO; along with Steve Young, Executive Vice President and Chief Financial Officer.

Today's discussion will include forward-looking information and the use of non-GAAP financial measures. Slide two presents the Safe Harbor statement, which accompanies our presentation materials. A reconciliation of non-GAAP financial measures can be found on www.duke-energy.com, and in today's materials.

Please note, the appendix for today's presentation includes supplemental information and additional disclosures. As summarized on slide three, during today's call, Lynn will provide an updates on recent activities including our response to Hurricanes Florence and Michael. She will also discuss progress on our strategic initiatives. Steve will then provide an overview of our third quarter financial results, and insight about economic and load growth trends. He will also discuss our growth drivers for 2019 before closing with key investor considerations.

With that, let me turn the call over to Lynn.

Lynn Good {BIO 5982187 <GO>}

Thank you, Mike, and good morning, everyone.

Let me begin on slide four. Today we announced strong results for the quarter with adjusted earnings per share are \$1.65 compared to \$1.59 in the prior year. We continue to execute on our strategic priorities, supported by the outstanding work of our employees who restored outages in back-to-back hurricanes over the last two months. As we look to the end of the year, we have narrowed our full year guidance to \$4.65 to \$4.85 per share, raising the midpoint into the upper half of our original range. We also reaffirmed our long-term earnings growth rate of 4% to 6% through 2022, also midpoint of our 2017 guidance range. We continue to expect earnings growth at the low end of this range in 2019, in the mid-to-high end of the range in 2020 and beyond.

In addition to strong financial results, we're pleased to highlight several recent recognitions for the company. Let me emphasize two that I know are important to our ESG investors. Duke Energy was included in the Dow Jones Sustainability Index for the 13th consecutive year, demonstrating our commitment to sustainability and corporate responsibility. And Forbes named Duke Energy to their Global Best Employers list, which is based on rankings of publicly traded companies from 60 countries around the world. We're proud that our company and employees are being recognized for the work we do everyday on behalf of our customers and communities.

Turning to slide five, I want to give you an update on our response to Hurricanes Florence and Michael. And in a moment, Steve will share our thoughts on cost estimates and recovery. First, Hurricane Florence. This is a massive slow-moving storm that made landfall on the North Carolina Coast in early September, causing wide-spread devastation and record-setting rainfall. Ahead of the storm, we assembled our largest restoration force ever in the Carolinas. Over 20,000 workers to prepare and immediately begin restoring power when it was safe to do so. In addition, 2,000 employees outside of transmission and distribution volunteered to support our efforts for managing logistics, to providing extra help, answering customer calls.

We restored over 1.8 million outages in less than 10 days with 93% restored in five days. Despite extensive flooding, the environment around our facilities including ash basins remained well protected. This is a testament to our team's extensive preparation in advance of the storm and on-the-ground management throughout the heavy rain falls.

Only weeks later Hurricane Michael made landfall in early October on the Florida, Panhandle, Michael triggered over 70,000 power outages in our Florida service territory before moving

North and causing over 1.1 million outages in the Carolinas. More than 15,000 workers contributed to the restoration efforts with 90% of the outages restored within three days. All customers who could receive power were restored in five days in the Carolinas and eight days in Florida, but work continues in Florida as we rebuild our infrastructure in the most devastated areas.

Our successful storm response was driven in part by lessons learned from previous storms and our investments to improve the grid. For example, in our DEP service territories, self-healing grid technologies rerouted power from damaged lines to minimize outages. We estimate that we avoided 27 million outage minutes across the Carolinas from the use of this technology during Hurricane Florence. Our grid improvement plan includes expansion of this technology to 80% of our customers over the next decade, up from 16% currently.

And in Florida, we made improvements on our transition line at St. George Island a few years ago. This area was in the direct path of the hurricane and the structures withstood hurricane force winds. During this hurricane season, we restored 3 million outages, thanks to the tireless work of our employees and utility partners, and I'm truly proud of this team.

The benefits of modernizing and hardening the grid were clear during the hurricanes and we continue to invest in the energy grid on behalf of our customers. We've highlighted several developments across our jurisdictions on slide six. In South Carolina, the commission approved deferral accounting treatment for our grid improvement investments such as smart meters, self-optimizing grid technology and additional hardening and resiliency mechanisms. Our grid improvement plan is a key part of our strategy to meet customer expectation. These investments will deliver increased reliability, enable distributed resources and providing enhanced customer convenience and control.

In the Carolinas, we've recently announced approximately \$500 million in battery storage investments over the next 15 years as described in our integrated resource plans filed this past September. This investment equal to about 300 megawatts of capacity that will provide our Carolinas utilities with another tool to balance the energy system.

In Florida, consistent with our multiyear agreement, we announced an electric vehicle pilot program that will install after 530 EV charging stations throughout our service territory in 2019. These stations will be connected in multi-unit dwellings, workplaces and other areas with broad public access. Similarly, we have proposed an electric transportation pilot in South Carolina which includes charging station programs to residential areas, as well as school and transit bus systems. We look forward to rolling out similar programs in our other jurisdictions to promote greater use of electric vehicles for our customers.

Moving to slide seven, let me provide an update on some of our other strategic investments. We are nearing completion of our 1,600 megawatt Citrus County natural gas combined cycle plant in Florida. The first unit came online in October. We have successfully achieved initial firing of Unit 2, which is on track to start serving customers in December.

Recall that the Florida Commission approved our requested \$200 million revenue increase for the plant under the GBRA mechanism, increases to customer rates for Unit 1 will begin in

December and rates associated with Unit 2 are expected to be implemented in January.

Construction continues at our natural gas combined cycle plant in Asheville as part of our Western Carolinas Modernization Project. The plant is 50% complete and remains on track for the expected late 2019 in-service date.

In July, we launched the first request for proposal for new renewable energy resources in North Carolina under House Bill 589. This 680 megawatt solicitation seeks projects that can be placed in service by the end of 2020. This was submitted October 9, including those from our North Carolina utilities and Commercial Renewables business. Over the next several months, the independent administrator will review the bids and winning proposals are expected to be notified in the first quarter of 2019. New project construction is anticipated to begin in the second half of 2019 to meet the 2020 in-service dates.

In commercial renewables, we started the process to find a minority partner in our existing 3,000 megawatt wind and solar portfolio as we seek to recycle and reinvest capital from these assets. We will continue to be the majority owner and operator of the portfolio, and tend to retain nearly all of the tax benefits associated with the projects. It is still early in the process but we are seeing strong interest.

Looking ahead to 2019, we have approximately 300 megawatts of wind and solar in late stages of development and we will use tax equity to finance these projects.

Turning to our gas business on slide eight, let me provide an update on the Atlantic Coast Pipeline. We're working diligently to complete the project to bring low cost gas supply and economic development opportunities to the region. Mainline construction continues in West Virginia and North Carolina, and we're making progress on constructing the compressor and metering in regulation stations in those states. The tree-felling window reopened in September and we continue with selling activities where permitted in all three states along the pipeline route. The Virginia DEQ approved our erosion and sediment control plan on October 19, making the water quality certificate effective for that state.

We've requested permission from FERC to begin full construction activities in Virginia and expect the approvals soon. This was the last major permit remaining for the pipeline, marking a significant milestone for the project. Throughout this process, the relevant permitting agencies have conducted extensive due diligence, ensuring the project will meet all necessary environmental rules and regulations. We appreciate the professionalism exhibited by these agencies as they worked with our project team to complete these reviews. Given permitting delays and the FERC's stop work order in August, the project partners have re-examined the construction schedule and cost estimate.

We will pursue with our customers, putting the pipeline in-service in phases for the late 2019 in-service for all station facilities and key portions of the pipeline in order to meet peak winter demand. We're also pursuing a mid-2020 in-service date for the remaining segments. Based on these changes, we now estimate cost in the range of \$6.5 billion to \$7 billion, an increase of \$500 million over the previous range. Future factors such as abnormal weather, work delays

due to judicial or regulatory action and other circumstances may result in additional cost or schedule changes.

In summary, our year-to-date results show that our company is performing well. We will continue executing on our strategy, investing in infrastructure, our customer's value and delivering sustainable growth for our investors. As we look to close out the year, our achievements once again reinforce our belief that Duke Energy is the leading energy infrastructure company.

And before I turn it over to Steve, I want to thank our employees once again for their remarkable work during Hurricanes Florence and Michael. They showed unwavering dedication to our customers.

Steve, let me turn it over to you.

Steven Young {BIO 7307044 <GO>}

Thanks, Lynn. I'll start with quarterly results on slide nine, including our adjusted earnings per share variances for the prior year. For more detailed information on variance drivers and a reconciliation of reported to adjusted results, please refer to the supporting materials that accompany today's press release and presentation.

On a reported or GAAP basis, 2018 third quarter earnings per share were \$1.51 compared to \$1.36 last year. Third quarter 2018 adjusted earnings per share was \$1.65 compared to \$1.59 in the prior year. The difference between reported and adjusted earnings was primarily due to a charge resulting from annual goodwill testing at our commercial renewables business.

For the quarter, higher adjusted results compared to the prior year were primarily due to higher retail electric sales volumes and income tax benefits, partially offset by higher storm restoration costs and share dilution. Within that segments, electric utilities and infrastructure was up \$0.10 compared to the prior year. Results were supported by a few factors, including strong load growth and more favorable weather. We also saw growth from higher rider revenues and contributions from the DEP and DEC North Carolina rate cases. Finally the electric segment benefited from lower income tax expense including impacts of the tax act.

These favorable drivers were partially offset by three items: higher depreciation and amortization expense from a growing rate base; a charge related to the Edwardsport settlement in Indiana and higher O&M largely due to Hurricane Florence restoration costs. We estimate total O&M for Hurricane Florence of approximately \$450 million with the majority of the costs at our DEP utility. We will request permission to defer approximately \$370 million of incremental cost for recovery in the next DEP rate case. The remaining incremental cost impacted O&M expense in the quarter and exceeded the cost from Hurricane Irma in 2017, contributing to the year-over-year variance.

I'd also point out that our preliminary O&M cost estimate for Hurricane Michael is approximately \$200 million. The cost from this storm which primarily impacted our DEC and DEF utilities will be recorded in the fourth quarter. As with Florence, we will also request to

defer the majority of these costs for future recovery. We will be making the appropriate filings with the state commissions over the coming months.

Shifting to gas utilities and infrastructure, results were flat in the quarter. Growth from our midstream investments was offset by higher O&M. We expect our LDC businesses to provide the bulk of their remaining earnings contribution in the fourth quarter.

In our commercial renewables segment, results were up \$0.03 for the quarter. The increase is primarily due to the Shoreham solar project, which was placed in service in July. Finally, Other was down \$0.04 in the quarter largely due to a lower tax shield as a result of the federal tax act and a favorable litigation settlement in the prior year. Higher tax optimization benefits partially offset these drivers. We continue to expect our full year 2018 adjusted effective tax rate to be in the range of 15% to 16%.

As you know we settled half of our March equity offering in June which resulted in \$0.03 of share dilution for the quarter. Our equity financing plan remains on track and we continue to expect to settle all outstanding equity forwards in the fourth quarter.

Our strong execution to the first three quarters gives us confidence in our full year projection. And as Lynn mentioned, we narrowed our 2018 guidance range to \$4.65 to \$4.85 per share, raising the midpoint into the upper half of our original guidance range for the year. This reflects our results to date including favorable weather, partially offset by costs associated with the two hurricanes. We are well-positioned for the remainder of the year and we'll manage our O&M and other business drivers in a way that keeps us on track to deliver on our commitments.

Turning to slide 10. Our retail volumes were very strong in the quarter. Let me take a moment to walk you through the trends we are seeing across our service areas. On a rolling 12 month basis, weather normalized, retail electric load growth was 1%. Our residential class continues to drive the growth with an overall increase of 1.8% on a rolling 12-month basis. Strong customer growth continues across our service territories and was amplified this quarter by positive usage per customer in certain jurisdictions. We will continue to monitor this trend, given we've seen this periodically over the course of the year.

We also saw strength in the commercial class with sales up 1.1% over the rolling 12 months. Ongoing data center expansion and strength in hospitality and leisure segments helped to offset weakness in retail stores driven by competition from online shopping. Finally, sales in our industrial class continue to improve and we were pleased to see a 1.8% increase within this sector during the quarter, driven by robust manufacturing growth in several sectors such as metals, textiles and transportation.

The Carolinas in particular saw strong industrial growth in the quarter. These retail volume trends along with a healthy economy and growth in our jurisdictions further support our long-term planning assumption of 0.5% retail load growth for our electric utilities.

As we head into the close of the year, let me highlight on slide 11 some of the drivers for 2019. We expect to be back within our long-term earnings growth range in 2019 which represents 6% growth off of our original 2018 midpoint. I'll start with growth in the electric utilities segment. In

the Carolinas, earnings will be supported by a full [ph] year's contribution from this year's North Carolina rate cases, upcoming rate activity in South Carolina as well as AFUDC on our Western Carolinas' Modernization Project.

In Florida, as Lynn discussed, we're adding the Citrus County combined cycle plant to customer rates in the next few months. We will also begin to recover our ongoing grid investments through the first rate increase under our multiyear rate plan. Finally we expect to initiate rate recovery under the solar base rate adjustment mechanism once our first solar project is in operation this December.

In the Midwest, we will continue to invest in transmission and distribution upgrades that are recovered under our rider program in Indiana and Ohio.

In the gas segment, earnings will grow based on the continued construction on the Atlantic Coast pipeline coupled with continued integrity management investments and strong customer additions in our gas LDCs. The changes to the ACP schedule and cost estimate that Lynn described will not significantly impact earnings in 2019 and 2020 as the project will continue to accrue AFUDC and now on a higher cost base. Additionally, we have a strong pipeline of projects in our commercial renewables business, including the late stage wind and solar projects with 2019 in-service dates.

Finally, we expect further load growth consistent with our long-term planning assumption and we are aggressively managing cost across our businesses including using digital capabilities to drive efficiencies. As you can see, we have a substantial set of investment opportunities that will provide growth into next year and beyond as we continue to execute on our strategy.

I'll close with slide 12. Our attractive investor value proposition is founded upon our growing dividend, which currently yields approximately 4.5% coupled with earnings growth of 4% to 6% from transparent low-risk investments. This provides a compelling risk-adjusted total shareholder return of 8% to 10%. Duke Energy's scale, constructive service areas and ability to execute position the company as the leading energy infrastructure investment.

With that, let's open the lines for your questions.

Questions And Answers

Operator

Thank you. (Operator Instructions) And we'll take our first question from Julien Dumoulin-Smith with Bank of America Merrill Lynch. Please go ahead.

Q - Unidentified Participant

Hi. Good morning. This is actually Claire for Julien here.

A - Lynn Good {BIO 5982187 <GO>}

Hi, Claire. And how are you?

A - Steven Young {BIO 7307044 <GO>}

Good morning.

Q - Unidentified Participant

Hi. Doing well. Thanks for taking my question. My first is just on ACP. What is your expectation on timing to fund that additional CapEx need? And how will it be funded? And what are you anticipating in the returns on ACP now are [ph]?

A - Lynn Good {BIO 5982187 <GO>}

So Claire, I'll take returns first. We expect this return to be consistent with other regulated investments. And so we're comfortable with where we are on return, and I would think about the financing of ACP is being managed through the overall financing of the company, and then we do intend to put project financing in place at the time the project goes in-service.

Q - Unidentified Participant

Okay. It doesn't really have much of a bearing on your FFO to debt metrics, just confirming that?

A - Lynn Good {BIO 5982187 <GO>}

We're committed to our FFO to debt metrics, Claire, and I think we've share this ranges with you in previous calls. The cost increase for ACP, our responsibility is about half of that amount and we believe we have tools within our companies to manage through that transition.

Q - Unidentified Participant

Got it. That's helpful. And just turning over to renewables as well, at this point, what do you think -- what you'd you estimate the market out there to be a potential or expected proceeds? And how would your use of proceeds work?

A - Lynn Good {BIO 5982187 <GO>}

Claire, we're very early in the process. What I'll share is that, there has been a strong interest. We've been watching this market for some time and are very familiar with it. The use of proceeds, I think we're too early to talk specifically about that. We haven't earmarked proceeds for any specific purpose. And of course, we'll update you as the sale process continues and give you a closer look at a financing plan as we come to the street in February.

Q - Unidentified Participant

Got it. Would it be fair to just view it as offsetting incremental debt issuances or any kind of other funding internally?

A - Lynn Good {BIO 5982187 <GO>}

I wouldn't be that specific at this point, Claire. We just launched the process, so we need to work through it in order to have a sense of where the market is, the proceeds, the timing and all of those things. So, that's where we are at this point.

Q - Unidentified Participant

Okay. Thank you. I appreciate it.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. We'll now take our next question from Jonathan Arnold with Deutsche Bank.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Good morning, guys. Thank you.

A - Lynn Good {BIO 5982187 <GO>}

Hi, Jon.

A - Steven Young {BIO 7307044 <GO>}

Good morning.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Just one quick thing. It looks like, if I look at trailing 12 months numbers, the midpoint of the new 2018 range would suggest a slightly down fourth quarter. Can you remind us what type of things would support that?

A - Steven Young {BIO 7307044 <GO>}

I think, as we go into the fourth quarter, you're looking at milder weather and that impact there will pick up gas distribution business. I don't think there's anything unusual that we're looking at in the fourth quarter. Some of the variations per quarter are hard to predict, tax optimization efforts as an example that came through in the third quarter, in certain years they've come through in a fourth quarter.

So I wouldn't look to anything negative that's occurring necessarily in the fourth quarter, Jonathan.

A - Lynn Good {BIO 5982187 <GO>}

And the only special thing I'd point to Jonathan is, Michael, it's in the fourth quarter. The strong hit in October. So we'll be addressing Michael in the fourth quarter.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Got you. And then, just on industrial growth you flagged last quarter that you're expecting some of the temporary effects to start working on to numbers, and it looks like that happened. But what do you feel is -- it's your underlying industrial sales growth number.

A - Steven Young {BIO 7307044 <GO>}

I think the underlying industrial sales growth number will continue to improve as we move out and lap, if you will, some of the unique probations there. We saw very strong industrial growth for this particular quarter as I mentioned across the entire enterprise of 1.8%. I don't know if we're going to see that as an ongoing mechanism -- ongoing number going forward, but we do see strength in our residential customers, a good bit of diversity across the enterprise. I don't have a full year number, I think the overall 0.5% is very solid but that combines residential with it and some commercial as well.

So no specific number yet on what I'd see industrial on a run rate but it's improving on the 12-month carrying. And I think, that will continue for a few quarters.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Yeah. My question really Steve was, is the growth -- the improvement is just the lapping of the outages or is it actually underlying growth as well?

A - Steven Young {BIO 7307044 <GO>}

I think, we're seeing some underlying growth as well with it.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Okay. And then, can you just remind us what is the sales growth assumption overall that underpins your comments on guidance and getting to the high end of 4% to 6% in 2020-plus?

A - Steven Young {BIO 7307044 <GO>}

Again, we're looking at 0.5% sales growth, weather normal across our footprint, and that's all customer classes. We continue to think, that's a reasonable number to bake in to our forecasting over our longer-term plans.

Q - Jonathan Arnold {BIO 1505843 <GO>}

Great. Thank you, guys.

A - Lynn Good {BIO 5982187 <GO>}

Thank you, Jonathan.

Operator

Thank you. We'll now move on to Michael Weinstein with Credit Suisse.

Q - Michael Weinstein {BIO 19894768 <GO>}

Hi, guys. Thanks for taking my questions.

A - Lynn Good {BIO 5982187 <GO>}

Hi, Michael.

A - Steven Young {BIO 7307044 <GO>}

Hello.

Q - Michael Weinstein {BIO 19894768 <GO>}

So just a follow-up on Jon's question. It looks like growth -- sales growth is actually continuing to improve and we've seen that for several quarters now and you're thinking that it might continue going forward. At what point do you think you might start considering increasing the projected growth that's embedded in guidance from 0.5% to something little higher?

A - Lynn Good {BIO 5982187 <GO>}

Michael, I think we'll continue to watch. We've been surprised to the upside, which is a good thing. But we believe, 0.5% assumption is good -- really established the parameters around our cost structure and the way we manage the business. For every positive piece of economic news, there is something on the horizon, whether it's tariffs or rising interest rates and other things. So we're really comfortable at 0.5% now and hope to surprise to the upside.

Q - Michael Weinstein {BIO 19894768 <GO>}

Got you. And the hurricane costs for Hurricane Michael and also for Hurricane Florence, is there anything else that's been going on? Those are being deferred right now and do you have a deferral order? Can you just remind me, sorry if I missed that earlier.

A - Steven Young {BIO 7307044 <GO>}

We will make application for the official deferral order in the near term. We are in the third quarter. We incurred the costs associated with Hurricane Florence. And as I said, we've deferred \$370 million of the O&M cost related to that, and the deferrals based upon past history and practice. We'll make those official filings later this year.

Q - Michael Weinstein {BIO 19894768 <GO>}

And as you get ready for next year's rate cases in North Carolina and also for -- talking to the state legislators about good modernization. Do you think that the, it would seem to me like an increasing frequency of hurricanes in your territory and throughout the Southeast. Is that being factored into the discussions or has that improved the climate for good modernization going forward?

A - Lynn Good {BIO 5982187 <GO>}

Yeah. Michael, I would say, those storms have been a significant issue here in the Carolina. It's just the impact on the Eastern part of the state and there is a lot of interest to invest in infrastructure to support that region and to mix more of investments to position the state for the future. So, I think hardening and resiliency is something that makes a lot of sense and we're of course developing projects that we believe would support the infrastructure and the state, taking lessons learned from these storms but also looking at other areas of our grid that we think modernization could benefit customers.

Q - Michael Weinstein {BIO 19894768 <GO>}

Thanks a lot, Lynn.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

We'll take our next question from Greg Gordon with Evercore ISI.

A - Lynn Good {BIO 5982187 <GO>}

Hi, Greg.

Q - Greg Gordon {BIO 1506687 <GO>}

Good morning. I have a -- going back to a lot of questioning from earlier, you're doing well this year. The midpoint of guidance is \$4.75 and then using a \$4.60 base, and I'm looking at slide 11, you're saying you expect the compound annual growth rate to be 4% through 2019. And then the compound annual growth rate not the incremental growth rate but the compound annual growth rate to more like 5% or 5.5% as you get into 2022. I just wanted to make sure that I'm looking at that correctly. You're using a compounding function, not a year-over-year function, correct?

A - Lynn Good {BIO 5982187 <GO>}

That's right. And so, Greg, what we're talking about is 4% compound number for 2019 and then by 2020 we believe we'll be up in that 5% -- mid-to-high end of the range.

Q - Greg Gordon {BIO 1506687 <GO>}

And that's my point. That's my point, because 5% compound from \$4.60 in 2017 to 2020 would put you \$0.10 above Street consensus, \$5.33 a share and it would put you \$0.15 above Street consensus in 2021. And so, I just and the Street has been consistently -- me included, to be frank with you more cynical about your growth opportunities as it pertains to your guidance. And so, what gives you the confidence that the compounding effect of the investments and the changes you're making in the business can get you there? And what do you think the differences between Street expectations and your aspirations?

A - Lynn Good {BIO 5982187 <GO>}

Greg, I would say that the capital plan that we've put in front of the Street is well with the recovery mechanisms that go with that, give us the confidence to deliver the results. And of course, cost management, load growth are also a part of that fixture. And we believe, we've been consistently demonstrating the ability to grow the company. This is the second full year of the portfolio that we now operate. Historically we had some noise with international and other things. We're now two years in the rear view mirror.

And my expectation is, as we continue to execute, there will be greater confidence that we will deliver what we've set out. And so we're proud of the fact that we're delivering what we set out in terms of commitments this year. We delivered last year. We've adjusted with tax reform in a way that has been constructive not only to investors but to the balance sheet. And so, our assignment is to keep executing in a way that it grows the company and maintain that balance sheet for the future, and that is our focus.

Q - Greg Gordon {BIO 1506687 <GO>}

Okay. And how necessary or important to the execution of your plan is, the grid modernization, capital plan roll out in North Carolina and getting recovery mechanisms even through a legislative guidance to the commission or from the commission that are a more contemporaneous return framework?

A - Lynn Good {BIO 5982187 <GO>}

Grid investment is an important part of the strategy, Greg. And certainly North Carolina is important to the results of Duke Energy because of the scale of those utilities, both DEC and DEP. As we've shared with you, we believe, we have parallel paths to pursue a legislative path or increased frequency of regulatory filings in order to achieve our financial results. We do believe with the value proposition that grid investment represents, including the storm hardening that we just talked about. But a recovery mechanism that is certain over a two year to three year period with predictable investment and predictable impact to customers with value that goes

with those predictable increases as a compelling business proposition. And we'll continue to pursue as I said in both the legislative and regulatory process.

Q - Greg Gordon {BIO 1506687 <GO>}

Lynn, thank you. Take Care.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. We'll take our next question from Stephen Byrd with Morgan Stanley.

Q - Stephen Byrd {BIO 15172739 <GO>}

Hi. Good morning.

A - Steven Young {BIO 7307044 <GO>}

Good morning, Stephen.

A - Lynn Good {BIO 5982187 <GO>}

Good morning, Stephen.

Q - Stephen Byrd {BIO 15172739 <GO>}

I wanted to go back to the ACP process given that the cost is going up. I wondered if you can just talk through the regulatory process for potentially adjusting the required revenue upward? Or should we assume that it's relatively unlikely that revenue will be adjusted upward. I just wanted to circle back on that?

A - Lynn Good {BIO 5982187 <GO>}

Stephen, I think we are in discussions with customers in connection with this partial in-service, trying to establish interim pricing. And our objective always is to find the right balance between meeting customer needs and delivering benefits, and then returns to investors. We have raised that price once and received approval of those prices. We believe, this investment still represents the most cost-effective solutions for our customers and we will continue to be in dialogue with customers as we go forward.

So our focus right now is on partial in-service and establishing interim prices and we'll just continue to stay in touch with customers as the project continues.

Q - Stephen Byrd {BIO 15172739 <GO>}

Understood. And then just further on system hardening. I think you've given us some good color as to how you're thinking about that. But I'm trying to get a better sense for the path to getting approval. So let's just say that you go through your assessment and you determine that an additional amount of capital is needed.

Could you talk a little bit more to the different paths that we should be thinking about in terms of getting approval for that spending? It just, it seems like obviously there probably are needs for significant additional hardening. How do we think about translating that into regulatory or legislative outcomes?

A - Lynn Good {BIO 5982187 <GO>}

Stephen, I think, it depends on the path that we take. I think in a legislative path, a stakeholder process will be important to have discussions around the type of investment, the timing et cetera. You may recall, we've reached a partial settlement with certain environmental stakeholders as part of the DEC case that set a term, a cap, pilots for target undergrounding and then specific investments around batteries, EV et cetera -- self-optimizing technologies et cetera.

So I think as you think about a multiyear rate plan or if you were to think about some other method to establish a multiyear investment program, there would be some degree of sharing those investments and agreement. We don't contemplate that we would necessarily be required pre-approval on individual process, because we're tracking about a number of small things that accumulate every time. But we of course are early in the process of making those changes.

Under a pure regulatory path, you make the investments and demonstrate benefits and those become a part of your cost of service and you would think about this in a traditional way. Let me just close by saying, we are in discussion around these investments and then benefits they can deliver to customers both with regulators and with stakeholders, and that process will continue. We think those investments are very important to the state and to our customer base. And so those conversations will continue.

Q - Stephen Byrd {BIO 15172739 <GO>}

Very good. Thank you very much.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. Now we'll take our next question from Steve Fleishman with Wolfe Research.

Q - Steve Fleishman {BIO 1512318 <GO>}

Hi. Good morning.

A - Lynn Good {BIO 5982187 <GO>}

Good morning, Steve.

Q - Steve Fleishman {BIO 1512318 <GO>}

Hi, Lynn. So just a question first on the quarter. I think in a couple of the businesses you mentioned the impact of tax rate partially due to the tax law change. Could you maybe separate out tax law change versus other tax items just so we have an idea on that?

A - Steven Young {BIO 7307044 <GO>}

Yeah. What I might mention here on tax law changes is, as we had some fixed price contracts at our wholesale business, gas and electric, whereby the pricing doesn't change necessarily due to tax changes. So that brings some benefits in. And then there's just tax optimization working through the various structures that we have in place across our footprint and provides some benefits. I don't have a breakout right now -- between those but those are the two factors that lead to it.

Q - Steve Fleishman {BIO 1512318 <GO>}

Okay, that's fine. And then I guess just on the renewables in North Carolina. My recollection is, those were not necessarily in your capital plan if you end up winning some of those but I'm not sure if anything else has kind of changed in the plan going back to really this year. So just, if we see you win a handful of projects there, should we think of that all being incremental or in the context of kind of the whole -- the plan, maybe something haven't gone away.

A - Lynn Good {BIO 5982187 <GO>}

I would think about it more within the context of the plan, Steve. We did have renewable capital in our plan in February. And actually the way we approach this is, we put all of the capital on the commercial business recognizing that it could either be in the utility or the commercial business depending on how we win but we put the capital in the commercial renewable segment.

So given the timeline of 589 and the fact we'll know more after the first of the year, we'll continue to update capital and share that with you in February. But I would think about it at this point as part of the overall capital plan that we shared with you.

Q - Steve Fleishman {BIO 1512318 <GO>}

Okay. Thank you.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. We'll take our next question Praful Mehta with Citi.

Q - Praful Mehta {BIO 19410175 <GO>}

Thanks so much. Hi, guys.

A - Lynn Good {BIO 5982187 <GO>}

Good morning.

A - Steven Young {BIO 7307044 <GO>}

Hello.

Q - Praful Mehta {BIO 19410175 <GO>}

So maybe first touch on the storms. I know, you're deferring some of the costs. But in terms of the cash flow, is there an ability to fund some of that cash with securitization? Or if there is an -- how do you fund or does it put any kind of pressure on the credit metrics or different funding GAAP given the storm cost that you're facing right now?

A - Lynn Good {BIO 5982187 <GO>}

Praful, we are financing in the short term with commercial paper, short-term financing methods. And we will convert to longer term at the right time. We'll be filing as Steve indicated for deferral at the end of the year and we'd like to match long-term financing with the recovery mechanisms that are in place.

We were always mindful of the impact to customers. And so we have tools like excess deferred taxes that have not yet been fully dealt with in the Carolinas securitization. As you mentioned, it is always a tool. So our plans will continue to mature on this over the balance of this year into next.

Q - Praful Mehta {BIO 19410175 <GO>}

Got you. And does commercial renewable and the sale of commercial renewable, will that fit neatly into it or does it happen to fit into it or is there a plan to kind of use some of those proceeds for this?

A - Lynn Good {BIO 5982187 <GO>}

We haven't earmarked proceeds from commercial renewable at this point, Praful. Early in the process, we don't yet know what the value is going to be, timing et cetera but you can think about that as a tool, right -- within the company at large, an inflow of cash. So we'll consider all of these things and really be in a position to give more feedback on specific financing plans in February.

Q - Praful Mehta {BIO 19410175 <GO>}

Got you. That's helpful. And then finally just following up a little bit on Greg's question on long-term growth. I wanted to understand, you had mentioned earlier, the impact of tariffs and other macro factors that could impact your growth as you think about it longer term. I guess, to achieve your long-term target, what are the variables we should be thinking about or tracking on a more macro level that we think -- that you think could impact your ability to execute on the 4% to 6%?

A - Lynn Good {BIO 5982187 <GO>}

Praful, those comments were within the context of, why not raise 0.5%? So we believe, 0.5% is a very good planning assumption as we look at the profile of our business where we're located geographically, the attractive nature of the service territories et cetera. But large economic shocks if we were to ever get to that point would be something we need to check and adjust but there's nothing unique to Duke Energy as I talk about that.

So as I think about long-term growth, 0.5% is the load growth assumption, aggressive cost management will continue to be a part of the equation. And then the capital plan we've put in front of you with rate increases or recovery mechanisms that are in place across our jurisdiction will be the other driver.

Q - Praful Mehta {BIO 19410175 <GO>}

Awesome. Very helpful. Thank you, Lynn.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. We'll take our next question from Shahriar Pourreza from Guggenheim Partners.

A - Lynn Good {BIO 5982187 <GO>}

Hi, Shahriar.

A - Steven Young {BIO 7307044 <GO>}

Hi, Shahriar.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Hi. Good morning, guys. You touched on most of my questions, but let me just -- can you just elaborate on 589 real quick and sort of what's embedded in your plan? Because, I thought prior communication really focused on having a very little -- somewhat of a base assumption around what you could win. And I guess, the way I'm trying to come up with this is, there's 2.7 gigawatts potentially in the state that can be procured. This 30% that you guys can essentially win but there's no cap on how much you guys can acquire from developers that are likely looking to recycle their capital, right?

So if you kind of look at the opportunity -- it could breach well over \$1 billion to \$2 billion of opportunity. So I guess my question is, how much of this is embedded in your plan? Is it sort of a very little base assumption? I'm just trying to figure out the scale here, because I thought this was predominantly incremental.

A - Lynn Good {BIO 5982187 <GO>}

Shahriar, I appreciate that question. We did put an assumption in but I think to use your terminology, it's going to be closer to our base assumption than it is to -- we buy everything assumption. And as I've said a moment ago, we're beginning to -- we're early in the process, the bids are in, the administrator will be reviewing this. We'll begin to have some visibility to this process in the first quarter and that would be the time for us to update. We see the nature of the projects, we see the returns that are implied and I think they represent great opportunities for us but we'll be evaluating those returns against the other investment opportunities we have and making good decisions about it.

So to close, I would say that the capital was in there is more of a base assumption.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Got it. And then just let me ask you assuming that the ultimate outcome is better than your base assumption. Do you see any need to -- for incremental equity as far as looking at additional opportunities around solar? So, i.e., if you do better than your base assumption, you acquire developers that are looking to recycle, is there any instance where you think you may need to raise equity as a result?

A - Lynn Good {BIO 5982187 <GO>}

Shahriar at this point we're comfortable with our plans we put in front of you on equity. The equity raise we did this year are ongoing assumptions around about \$350 million of equity a year. We think that positions the company really well, strike the right balance between balance sheet and growth.

And so, I would think about that incremental capital is being evaluated as part of our total investment plan and we'll continue as I said to provide updates on where -- what we think the future holds. But right now, I'm comfortable with the equity plan we have in place and our

ability to absorb upside on the renewables as we look at the total collection of capital that we are planning to spend as a company.

A - Steven Young {BIO 7307044 <GO>}

And I'd add that the use of tax, equity financing and bank leverage and so forth helps on minimizing the investment on commercial renewables.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Got it. Thanks, Steven; and see you soon.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. We'll take our next question is from Ali Agha with SunTrust.

Q - Ali Agha {BIO 1509168 <GO>}

Thank you. Good morning.

A - Lynn Good {BIO 5982187 <GO>}

Good morning.

Q - Ali Agha {BIO 1509168 <GO>}

Good morning. First question, I wanted to just clarify the race [ph] in the 2018 midpoint of \$0.05, is that all primarily driven by better weather or was there something else in there?

A - Lynn Good {BIO 5982187 <GO>}

Ali, I would say weather and volumes on the upside really being offset by storm expense is the way I would look at it. So we've had very strong weather and volumes but we've also have the hurricanes to absorb.

Q - Ali Agha {BIO 1509168 <GO>}

I got you. Okay. And secondly, next year, Lynn, when you all update your plans et cetera, is there a thought would you move your base year to 2018 to build out your growth rate targets? Or what are you thinking about there?

A - Lynn Good {BIO 5982187 <GO>}

Ali, we haven't made a decision around base year, we've been working off of 2017. As you know we continue to emphasize that as outlined on slide 11. So we will make that evaluation as we go forward but you should be comfortable that we are talking about a range that works off of the 2017 base.

Q - Ali Agha {BIO 1509168 <GO>}

Yeah. And then also in terms of the longer-term growth outlook, just remind us again sort of embedded in your long-term 4% to 6% CAGR, how much reduction if any in regulatory lag is assumed in there? Or is it sort of CapEx rate base driven with earned ROEs relatively constant. Can you just remind us what beyond ROE trends?

A - Steven Young {BIO 7307044 <GO>}

A couple of things, I'd point out. We've got a long history of earning well on our regulated rate basis -- 10%, 10.5% range through periods of having rate cases, not having rate cases, we've been able to utilize cost efficiencies, expansion of wholesale and rate cases to make that happen through various differing circumstances. There certainly is an element of lag as you build your investment base between rate cases. That's natural to occur. It will vary depending on the regulatory mechanisms in place and the timeframes between rate cases. But we're working to reconstruct the regulatory recovery mechanisms and minimize lags as much as possible.

Q - Ali Agha {BIO 1509168 <GO>}

Okay. Steve, so just to be clear, that ramp up -- the implied ramp up in growth from 2020 onwards, that's all being driven by the way you're looking at your CapEx profile? You're not assuming a pickup in earned ROE, helping you in '20 and beyond?

A - Steven Young {BIO 7307044 <GO>}

Well. I was looking at the investment base growing and our ability to convert that into revenues in the regulatory processes. In addition to organic load growth and our renewables business, all of that combine. But on the regulated side, it's the investments and the ability to efficiently incorporate that into revenues at typical allowed types of returns as we have demonstrated our ability to do for many years.

Q - Ali Agha {BIO 1509168 <GO>}

Understood. Thank you.

A - Lynn Good {BIO 5982187 <GO>}

Thank you.

Operator

Thank you. And our final question today comes from Michael Lapides from Goldman Sachs.

Q - Michael Lapidès {BIO 6317499 <GO>}

Hey, guys. Thanks for taking my question. I look forward to --

A - Lynn Good {BIO 5982187 <GO>}

Hi, Michael.

Q - Michael Lapidès {BIO 6317499 <GO>}

Hi, Lynn. I have an easy one. You filed in South Carolina, can you talk to us a little bit about just your main request in South Carolina and whether you're actually trying to seek any kind of more structural change in ratemaking there? Or is it kind of a traditional rate case? And then B, how should we think about where you're likely -- the cadence of rate case filings between now and maybe the end of 2019 in terms of where you're likely to file?

A - Lynn Good {BIO 5982187 <GO>}

Michael, I would think about the South Carolina cases as mirroring in many ways what we try to accomplish in North Carolina. So the same drivers and approach trying to focus on grid investment but also receiving recovery to historic investments that will be the same approach in South Carolina.

We did point out in this call that we were successful in achieving a deferral of the grid investments which we view as a positive step in South Carolina. And then in terms of other rate cases, Florida will automatically reset with the Citrus, the solar and the grid investment. Midwest also will continue to reset, but you can expect us to file cases next year. Piedmont potentially, Indiana potentially and then with the in-service date of Western Carolinas. That's a good date to watch for the Duke Energy progress case.

Q - Michael Lapidès {BIO 6317499 <GO>}

Got it. Thank you. And I guess last one, how do you think about the cadence of O&M in 2018 relative to what you originally expect? And I'm trying to think about it excluding storm impact. And then, the opportunity set for being able to manage it down further in 2019.

A - Steven Young {BIO 7307044 <GO>}

In 2018, we're tracking to be right at our target for O&M exclusive of the storm cost. And again our broad target for our O&M is to keep it flat throughout our planning horizon. And I think we have the capabilities to do that -- to do better than that as we advance capabilities and data analytics and rolling out digital technology capabilities across our footprint. With our scope and scale, I think we have great abilities to control O&M.

Q - Michael Lapidès {BIO 6317499 <GO>}

Got it. Thank you, Steven. Thank you, Lynn. See you out in California.

A - Lynn Good {BIO 5982187 <GO>}

All right.

Operator

Thank you. And that does conclude today's question-and-answer session. I would like to turn the conference back over to Ms. Lynn Good for additional or closing remarks.

A - Lynn Good {BIO 5982187 <GO>}

Great, thank you. And thank you again for your interest and investment in Duke Energy. We look forward to seeing many of you in the upcoming EEI Conference next week. So, thanks again.

Operator

Thank you. And that does conclude today's conference. Thank you all for your participation.

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