Q2 2023 Earnings Call

Company Participants

- David McFarland, Vice President, Investor Relations
- Robert M. Blue, Chair, President and Chief Executive Officer
- Steven Ridge, Chief Financial Officer

Other Participants

- Carly Davenport, Analyst, Goldman Sachs
- Jeremy Tonet, Analyst, JP Morgan
- Shahriar Pourreza, Analyst, Guggenheim Partners

Presentation

Operator

Welcome to the Dominion Energy Second Quarter Earnings Conference Call. At this time, each of your lines is in a listen-only mode. At the conclusion of today's presentation, we will open the floor for questions. Instructions will be given for the procedure to follow if you'd like to ask a question. I would now like to turn the call over to David McFarland, Vice-President of Investor Relations.

David McFarland {BIO 20946446 <GO>}

Good morning, and thank you for joining today's call. Earnings materials, including today's prepared remarks, contain forward-looking statements and estimates that are subject to various risks and uncertainties. Please refer to our SEC filings, including our most recent Annual Reports on Form 10-K and our Quarterly Reports on Form 10-Q for a discussion of factors that may cause results to differ from management's estimates and expectations. This morning, we will discuss some measures of our company's performance that differ from those recognized by GAAP. Reconciliation of our non-GAAP measures to the most directly comparable GAAP financial measures, which we can calculate are contained in the earnings release kit. I encourage you to visit our Investor Relations website to review webcast slides, as well as the earnings release kit.

Joining today's call are Bob Blue, Chair, President, and Chief Executive Officer; Steven Ridge, Senior Vice-President, Chief Financial Officer; and Diane Leopold, Executive Vice-President and Chief Operating Officer. I will now turn the call over to Bob.

Robert M. Blue {BIO 16067114 <GO>}

Thank you, David. Good morning, everyone. As announced this morning, we reported second-quarter operating earnings of $0.53 per share. Our results were meaningfully impacted by historically mild weather and outages at the Millstone Power Station, both of which will address later in our prepared remarks. But first, I'll address our safety performance and provide an update on the status of the business review. Turning to Slide 3, our employee OSHA injury recordable rate for the first half of the year was 0.32%, this remarkable performance has us on pace to achieve the best safety year in the history of our company. Safety is of course much more than just a number on a page. It's our first core value and represents the well-being of our people. I commend my colleagues for the dedicated focus necessary to create and maintain the safety mindset and work practices that enable this outstanding performance.

Moving now to the business review. I'm pleased with the progress we're making toward delivering a compelling repositioning of our company to create maximum long-term value for shareholders, employees, customers, and other stakeholders. As I've said before, I'm as excited as ever for the future of our company. Our guiding commitments and priorities are unchanged and replicated identically on Slide 4. The review timeline shown on Slide 5 is also unchanged. We expect to conclude the review and host an Investor Day during the third quarter, at which we will provide an updated strategic and financial outlook for the company. We are working expeditiously but conscientiously in recognition of the vital importance of achieving an optimal result. Since announcing the review last November, we have among other steps, rigorously engage with our shareholders to listen, reflect, and inform our business review commitments and priorities.

We're committed to maintaining a similar level of engagement as we navigate through and beyond the review. We know that rebuilding trust is vital. We've positioned Dominion Energy for long -- Dominion Energy, Virginia, for long-term success by working collaboratively with key stakeholders to simplify the regulatory framework, provide meaningful rate relief to customers, and ensure the stability that will allow our company to confidently continue to allocate billions of dollars of annual investment in support of the economic prosperity of the citizens of the Commonwealth of Virginia, to the benefit of both customers and capital providers. We've confirmed our commitment to the current dividend. We've committed to and taken steps to improve operating earnings quality. We continue to focus on cost control by looking for what more can be done without losing sight of the absolute necessity of meeting high customer service standards and against the backdrop of the significant operational and cost efficiencies we've achieved over the last several years.

So consistent with prior comments, while there may be some potential in that area, we do not see it as a game-changer. We've included our O&M performance metrics in the appendix of today's materials for reference. And we've committed to improved credit profile and taking the first step toward that goal by announcing an agreement to sell our remaining interest in Cove Point, which will generate approximately $3.3 billion of cash after tax, which we will use to reduce debt. This highly credit-accretive transaction was the result of a robust and competitive sale process. The sale represents an attractive exit from what is been an excellent investment for our shareholders. With this sale, we've recycled nearly $9 billion of cash flow since 2018, which is well in excess of our total investment in the facility, inclusive of the export project construction costs of approximately $4 billion. We've included the investor slides we published at the time of the announcement in the appendix of today's materials. The request for HSR clearance and the DOE notification of both have been filed, and we expect the transaction to close later this year. We will continue to announce updates as events warrant as we work to finalize additional business review inputs in advance of the Investor Day.

With that, I'll turn it over to Steven to address financial matters.

Steven Ridge {BIO 20475546 <GO>}

Thank you, Bob, and good morning. Our second-quarter 2023 operating earnings as shown on Slide 6 were $0.53 per share. As you're aware, we revised our second-quarter guidance on June 30 from a range of $0.58 to $0.68 per share to a range of $0.44 to $0.50 per share to reflect our expectation for the negative impact of weather and unplanned outages at Millstone. First on weather, I'll just note that second-quarter weather was the mildest relative to 15-year normal in the last 50 years and amounted to an $0.08 headwind during the quarter. With regard to Millstone, we experienced both an increase to the duration of a planned outage at Unit 2 and an extended unplanned outage at Unit 3, which taken together amounted to an additional $0.08 headwind during the quarter. These outages are uncharacteristic for Millstone, which has a strong history as the largest zero-carbon electricity resource in New England of exemplary safety and reliability performance.

Senior leadership, including Eric Carr, who recently joined as our new Chief Nuclear Officer, after several years at PSEG, most recently as their Chief Nuclear Officer, has instituted a thorough and peer-involved review of the plant operating practices to ensure that despite the unusual nature of these outages, the station is prepared to consistently operate at its maximum potential for years to come. Higher sales and lower O&M contributed to the modest outperformance relative to the revised guidance range. Relative to the second-quarter last year, positive factors include higher sales and O&M timing. Negative factors include higher interest expense, lower DEV margins for certain utility customer contracts with market-based rates, higher depreciation, the absence of solar investment tax credits, and as discussed weather and Millstone.

Second-quarter GAAP results reflect a net income of $0.69 per share, which includes the positive non-cash mark-to-market impact of economic hedging activities and unrealized gains in the value of our nuclear decommissioning trust funds. A summary of all adjustments between operating and reporting [ph] results is included in Schedule 2 of the earnings release kit. Moving now to guidance on Slide 7. Given the pending business review, we are not providing full-year 2023 earnings guidance. For the third quarter 2023, we expect operating earnings to be between $0.72 and $0.87 per share. Last year's third-quarter operating earnings were $1.11 per share. Let me walk through some of the key drivers of this year-over-year change, all of which we've identified previously. First, approximately $0.12 from higher interest expense as a result of higher market rates. Approximately, $0.09 related to the $350 million Rider revenue reduction, which became effective July 1.

Approximately, $0.06 related to the removal of Cove Point from operating earnings effective July 1, due to the sale agreement. About half of that is related to the absence of a $0.03 help this quarter relative to last year from higher variable revenue and other additional services. This number also doesn't capture the impact of expected lower interest expense due to parent debt retirement from sale proceeds later this year, which we estimated approximately $0.05 to $0.06 per share on an annualized basis. Approximately, $0.04 from the elimination of non-regulated solar investment tax credits and approximately $0.02 from an O&M related to the Millstone fall planned outage. Before moving to sales trends, let me emphasize one of our business review priorities. A durable high-quality and predictable long-term earnings growth profile with consistent execution, we recognize the critical importance of meeting any post-review financial targets, even if and when unexpected headwinds occur.

Turning to Slide 8, I'll address electric sales trends. When we announced the review in November, we described the long-term scope and duration of our resiliency and decarbonization capital investment opportunity as very much intact. In May, we discussed PJM's updated electric load projections that forecast summer low growth in the Dom Zone of 5% per year for the next 10 years. Those estimates reflect the very robust demand growth we're observing in real-time across our system. Weather-normalized sales in Virginia increased 5% over the last 12 months through June as compared to the prior year. For full-year 2023, we expect the growth rate at the DEV to be around 5%. It's worth noting that just last week, we registered new summer peak demand records on consecutive days, and just as we expect our customers likely would have no idea given the high-quality operational performance delivered by our colleagues under these demanding load conditions. The unique intersection of industry-leading demand growth and strong policy support for resiliency, decarbonization, affordability, and economic growth, combined with the durability of the Virginia regulatory structure, represents an unprecedented opportunity for our company, our customers, and our capital providers.

It will drive growth for many years to come, demand prudent capital allocation and require a strong balance sheet, which brings me to my next topic, credit. Our commitments and priorities with regard to credit are unchanged, I'll reiterate them here. As we've discussed, despite meaningful qualitative improvement over the last several years, our credit metrics need strengthening. We want to emerge from the review with the ability over time to consistently meet and exceed our downgrade thresholds even during temporary periods of cost or regulatory pressure. As part of the review, we're analyzing the most efficient sources of capital to improve our balance sheet and fund our robust capital investments, while seeking to minimize any amount of external equity financing need. As Bob mentioned, the Cove Point transaction was strongly credit accretive, improving consolidated FFO-to-debt as measured by Moody's by 70 basis points.

Post-sale comments by the rating agencies with whom we maintain frequent engagement highlighted the credit-positive nature of the announcement but noted, as we expected that additional steps are required to ensure that our metrics sustainably meet and exceed our downgrade thresholds going forward. As it relates to credit, the objective of the business review is to create a robust balance sheet foundation that can both withstand potential temporary headwinds and also sustainably support the significantly elevated levels of regulated capital investment over the next few years.

With that, I'll turn the call back over to Bob.

Robert M. Blue {BIO 16067114 <GO>}

Turning to Slide 9, let me start by updating you on the implementation of the Virginia rate reform legislation that became effective on July 1. The New Virginia law provides significant bill relief for our customers and supports the long-term stability of our largest utility segment. With nearly unanimous bipartisan support, the legislation provides the certainty we need to fund and execute the critical energy investments that support the robust electrical demand growth in

Virginia. As of July 1, the law directly enabled a nearly $14 reduction to the typical Dominion Energy residential customer's monthly bill. Roughly, half of this decrease results from the cessation of certain riders that represent approximately $350 million of annual revenues. The other half of the reduction comes from a downward adjustment to the component of electric rates, that recovers the cost of power station, fuel, and purchase power. The commission has allowed this interim adjustment to take effect, while it considers the fuel securitization proposal, DEV filed on July 3.

By arranging for certain unrecovered fuel cost to be paid-off over time, securitization would avoid the possible alternative, an abrupt rate increase that would amount to about $15 per month for typical residential customers. We expect a final order by early November. DEV also submitted its biennial review filing on July 3, initiating a review of base rates, which represents about one-third of DEV's total rate base. The filing highlights DEV's exceptionally reliable and affordable service. Consider these facts, 99.9% average reliability delivered at rates 22% below the national average. I note, our track record of operating efficiently is reflected in our competitive rates as I mentioned previously. Since 2010, the typical residential bill has grown by only about 1.2% year-over-year, less than half of the 2.6% increase in the general inflation rate. We're proud of our record and the work we do to serve customers every single day. We expect a final order by March 3 of next year.

Turning to offshore wind on Slide 10. The project remains on-time and on-budget, consistent with the timelines and estimates previously provided. We continue to work closely with the Bureau of Ocean Energy Management and other stakeholders to support the project's timeline. BOEM received comments from all agencies on the draft of the final EIS and is on schedule to deliver the final EIS by the end of September, and the record of decision by the end of October. We continue to be encouraged by the administration's timely processing of offshore wind projects. In July, the SCC approved our updated offshore wind rider. In the application, DEV requested and received an annual revenue requirement of $271 million for jurisdictional customers. I'm pleased to update that our current project costs, excluding contingency, are now more than 90% fixed. Our procurement and manufacturing processes are well underway. In fact, we expect the first monopiles to be delivered to the port of Virginia later this year.

Our current contingency reserve is still about equal to our original reserve, despite having progressed the project significantly and fix more costs. Taken together and despite trends we see elsewhere in the offshore wind market, we do not see anything that changes our confidence in delivering the project on-time and on-budget. Project to date, we've invested approximately $1.7 billion, which we expect to grow to around $3 billion by year-end. As a reminder, we updated our expected LCOE and our most recent regulatory filing to the low-end of the $80 to $90 per megawatt range to account for PTC value-based on the Inflation Reduction Act. Our Jones Act-compliant installation vessel is currently 74% complete. No change to our expectation of completion well in advance of the need to support the currency of our construction schedule and timely completion by the end of 2026. Turning to other notable updates on Slide 11. We've continued to see strong regulatory outcomes related to nuclear life extension, clean energy, and grid transformation. On data centers, we continued to advance a series of infrastructure upgrade projects that will enable incremental increases in power for data center customers in Eastern Loudoun County.

Four projects have been completed ahead of schedule. An additional project is on-schedule to be completed by the end of 2023. We continue to develop a new 500 kV transmission line with an expected in-service date of late 2025. Given the unprecedented growth in areas served by our electric transmission, we continue to see an acceleration of and long-term increase in electric transmission investment opportunity throughout our service area. As such, we recently submitted a significant number of additional projects as part of PJM's transmission planning process, that we believe will ensure the electric grid in Virginia is reliable, resilient, and able to adapt to the increasing energy demand, while also transitioning to cleaner energy resources. Turning to Dominion Energy, South Carolina, on Slide 12. In addition to delivering safe and reliable energy, DESC's electric rates for residential customers are 9% below the national average as of July 1. We're proud to meet the energy needs of the robust economic development and population growth in South Carolina. On the regulatory front, we'll complete the testimony and hearings phases in our natural gas general rate case in the next few weeks. We expect an order from the commission by October. Following commission approval of the electric fuel settlement, the annual fuel adjustment was effective in May, and is designed to eliminate all previous under collections during this fuel year.

Finally, at our Gas Distribution business. Strong economic development is driving attractive customer growth year-over-year of 2.4% in North Carolina and 2.3% in Utah. Across all our gas businesses, we continue to see strong support for timely recovery on prudently incurred investments that provide safe, reliable, affordable, and increasingly sustainable service, including pipeline replacement efforts and expansion of service to rural communities. On RNG, we have six RNG projects currently injecting gas, with 18 other projects in various stages of development. With that, let me summarize our remarks on Slide 13. Our safety performance this quarter was outstanding. We reported operating earnings of $0.53 per share. We continue to execute on our decarbonization and resiliency investment programs to meet our customers' needs while creating jobs and spurring new business growth. Our offshore wind project continues to move forward on-schedule and on-budget and the business review is proceeding with pace and purpose. I'm focused on ensuring that Dominion Energy is best-positioned to create significant long-term value for our shareholders.

With that, we're ready to take your questions.

Questions And Answers

Operator

Thank you. At this time, we will open the floor for questions. (Operator Instructions) And our first question comes from Shahriar Pourreza with Guggenheim Partners.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Hey, guys, good morning.

A - Robert M. Blue {BIO 16067114 <GO>}

Good morning, Shar.

A - Steven Ridge {BIO 20475546 <GO>}

Good morning, Shar.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Good morning. Bob, just as one of my favorite questions to ask you is, obviously, as we're getting closer to the Investor Day, I guess is there any changes to your expectations for kind of this turnkey event now that you've sold Cove or could there still be some contingencies on potential ongoing sale processes? So with all of our questions be answered as we think about the balance sheet, base earnings growth rate, et cetera, as we head into that event.

A - Robert M. Blue {BIO 16067114 <GO>}

Yeah, no change, Shar, and we would expect to your questions to be answered. As we've said, our objective is to eliminate as many input variables as possible by the time we get to that Investor Day, and we're on track to do that, so no change.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Okay, good. And then, it's good to see on the offshore wind you guys have locked-in additional costs there. And I don't need to like ask a blunt question like this, but it might as well, but can you just tell us if you've had any interest in the wind stake option at all at this point, just given what we've been seeing around?

A - Robert M. Blue {BIO 16067114 <GO>}

Yeah, Shar, as we've said throughout the business review, we're reviewing from top-to-bottom, taking a look at everything in the business. By statute, there is an option for us related to offshore wind and we're reviewing that as part of the business review, but I can't update you anymore on it.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Okay, okay. And then, just lastly, one of the Millstone units obviously heading for another outage this fall, I mean, can you just talk about sort of talk to the quantum, like that O&M there and it seems like there has been some issues with the units this year, is there any kind of major capital investments you may be facing there? Thanks.

A - Steven Ridge {BIO 20475546 <GO>}

Shar, this is Steve, I'll take, with regard to the fall outage I mentioned we'll see about $0.02 of that hurt in Q3 and the remainder of the hurt in Q4. It's fairly standard. Think about, typical planned outage is about a $50 million O&M hurt given how we accelerate that work during that time period. And then of course on top of that, there is loss margin from that unit not actually producing electricity to sale. But there's nothing unusual about the planned outage in the fourth quarter. As I mentioned, the performance of Millstone in the second quarter is very uncharacteristic and it was something we're taking very, very seriously as I mentioned in the prepared remarks. Those units will continue to operate at very high reliability going forward. There was no fundamental issue that we discovered that we expect is going to require massive amounts of capital investment going forward to remediate going forward.

Q - Shahriar Pourreza {BIO 15145095 <GO>}

Okay, all right, perfect, guys, that's all I had, so we wait for the Q3 update. Thanks, appreciate it.

A - Robert M. Blue {BIO 16067114 <GO>}

Thanks, Shar.

Operator

And our next question comes from Jeremy Tonet with JP Morgan.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Hi, good morning.

A - Robert M. Blue {BIO 16067114 <GO>}

Good morning, Jeremy.

A - Steven Ridge {BIO 20475546 <GO>}

Good morning, Jeremy.

Q - Jeremy Tonet {BIO 15946844 <GO>}

I was just wondering if you could help me -- help me out a bit with I guess earnings trajectory for the business overall. If we look at kind of year-to-date results in 3Q guide, and the 4Q is flat year-over-year, it seems like it's down a bit year over here and so I'm just wondering if you could share any other thoughts as far as trajectory and what could revert next year to may -- with '24?

A - Steven Ridge {BIO 20475546 <GO>}

Hey, Jeremy, it's Steve. That's really good question, thanks for that. So let me start with this, at the Investor Day, which we intend to have in the third quarter, we're going to provide very clear direction on our company's post-review earnings and earnings growth outlook, including a buildup of the parts to that consolidated forecast. I would just say that 2023 is very much a transition year for us and I understand that it does make it more challenging to model. But since the initiation of the review, I think we've tried to be very transparent as we've delivered results around key drivers that are going to impact 2023 results, including the DEV rider role and interest expense, and we don't see that those major categories have changed much. So we haven't given full-year guidance as we mentioned, but I would say we're cognizant of investment community's interest in what the earnings potential of the company is going to be and the good news is that we're going to be very comprehensive in how we address that as part of the Investor Day.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Got it, makes sense. We will stay tuned for that. Maybe looking in the rear-view at this point if you're able to offer more commentary in Virginia now with being approved, what is the reaction from regulators and stakeholders then to the DEV rate reduction there? Just trying to get a temperature check on everything in Virginia.

A - Robert M. Blue {BIO 16067114 <GO>}

Yeah, as you would expect people are pretty positive about a rate reduction. I think that if you look at the history of our regulatory outcomes in Virginia over the last few years, you see approval of the variety of new clean energy programs, approval of subsequent license renewal investments, approval of transmission projects, we've I believe worked well with stakeholders and the regulatory process and achieved strong outcomes. And I think if you look at the big-picture, as we mentioned in our prepared remarks, our reliability is high, our rates are competitive, substantially below the national average, that's a very good place to be when you're in front of your regulators.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Got it, that's very helpful. I'll leave it there. Thanks.

A - Robert M. Blue {BIO 16067114 <GO>}

Thanks, Jeremy.

Operator

And our next question comes from Carly Davenport with Goldman Sachs.

Q - Carly Davenport {BIO 21913922 <GO>}

Hey, good morning. Thanks for taking the questions. Wanted to just start off on the demand side, do you feel PJM's peak forecast kind of accurately capture the growth that you're seeing in Virginia? And maybe how do you think about that in the context of your forecast for electric sales growth in Virginia going forward? It seems like it's pretty in line for 2023, but just kind of as you think about 2024 and beyond.

A - Robert M. Blue {BIO 16067114 <GO>}

We've spent a lot of time talking to PJM over the last few years on what we're seeing in terms of data centers and we believe that is reflected in their most recent sales forecast, which is robust. But we're seeing robust interest and as we described in our prepared remarks, we're seeing strong demand growth this year in line with what we would expect over the course of the next few years. There's just no evidence that we can see that this kind of growth is abating, where more and more interest from data center customers in our service territory and so I would say the PJM forecast is pretty reflective of what we expect the future will look like.

Q - Carly Davenport {BIO 21913922 <GO>}

Great, that's helpful. And then, maybe just a follow-up kind of, I appreciate all the updates that you provided on Virginia, just wanted to touch on the nuclear life extension program. Can you just talk about kind of what investments are included in that initial $1.2 billion? And then what other potential phases of that program could look like?

A - Robert M. Blue {BIO 16067114 <GO>}

Yes, so the overall investment we expect to be $4 billion and it is a variety of programs. A chunk of what's in that early $1.2 billion for example is, we have a lot of big piping at our stations that we've put up sort of carbon, fiber inlay, and that will allow them to be quite reliable for many, many years. There are -- the host of other projects, large and small, that will be included in that $4 billion, but will put us in a strong position to be able to operate at North Anna and at Surry for an additional 20 years. We can give you some more specific detail post-call if you're looking for it, we've got that in the filings.

Q - Carly Davenport {BIO 21913922 <GO>}

Great. Thanks so much. I'll leave it there.

Operator

Thank you. This does conclude this morning's conference call. You may now disconnect your lines and enjoy your day.