Company Name: Dominion Energy Inc
Company Ticker: D US
Date: 2017-08-02
Event Description: Q2 2017 Earnings Call

Market Cap: 49,674.06
Current PX: 77.19
YTD Change($): -3.87
YTD Change(%): -4.774

Bloomberg Estimates - EPS
Current Quarter: 0.886
Current Year: 3.578
Bloomberg Estimates - Sales
Current Quarter: 3349.000
Current Year: 12833.300

Q2 2017 Earnings Call

Company Participants

- Thomas E. Hamlin
- Mark F. McGettrick
- Thomas F. Farrell II
- Paul D. Koonce

Other Participants

- Michael Weinstein
- Shahriar Pourreza
- Stephen Calder Byrd
- Steve Fleishman
- Jonathan Philip Arnold

MANAGEMENT DISCUSSION SECTION

Thomas E. Hamlin

GAAP and Non-GAAP Financial Measures

Also on this call, 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 we are able to calculate and report are contained in the earnings release kit and Dominion Energy Midstream's press release

Mark F. McGettrick

Financial Highlights

Operating Earnings

- Dominion Energy reported operating earnings of $0.67 per share for Q2 2017, which was in the upper half of our guidance range
- Positive factors vs. guidance for the quarter were lower operating expenses, and income taxes, while the principal negative driver continued to be below normal weather

GAAP Earnings

- In fact, the earnings impact of mild weather during H1 was $0.10 per share
- GAAP earnings were $0.62 per share for Q2

- The principal difference between GAAP and operating earnings for the quarter were charges related to our integration of Questar
- A reconciliation of operating earnings to reported earnings can be found on Schedule 2 of the earnings release kit

Results by Operating Segment

Power Delivery

- Moving to results by operating segment
- Power Delivery produced EBITDA of $422mm for Q2, which was in the middle of its guidance range
- The impact of mild weather was offset by lower operating expenses

EBITDA

- EBITDA at Power Generation was $554mm, also in the middle of its guidance range
- Offsetting the weather impact were lower operating and maintenance expenses
- Gas Infrastructure produced EBITDA in the upper half of its guidance range at $423mm
- Higher transportation and distribution margins were the principal drivers of the strong results
- Overall, we are very pleased with the results of our operating segments
- For Q2 2017, Dominion Energy Midstream Partners produced adjusted EBITDA of $68.6mm which was two times the level produced in Q2 last year

Cash Flow

- Distributable cash flow of $40.7mm was 70% higher than the level of last year's second quarter
- The acquisition of Questar Pipeline in December of last year was the principal driver of the increase
- On July 21, Dominion Energy Midstream's Board of Directors declared a distribution of $0.288 per common unit payable on August 15
  - This distribution represents a 5% increase over last quarter's payment and is consistent with our 22% per year distribution growth rate plan
- Our coverage ratio remains extremely strong at 1.24 times

Treasury Activities

- Moving to treasury activities
- Cash flow from operating activities was $2.4B for Q2
- We have $5.5B of credit facilities
- And taking into account, cash, short-term investments, and commercial paper outstanding, we ended the quarter with available liquidity of $2.7B.
- For the status of our 2017 financings, please see slide 7

- And for statements of cash flow and liquidity, please see pages 14 and 25 of the earnings release kit

Hedging

- As to hedging, you can find our hedge positions on page 27 of the earnings release kit
- We have hedged 95% of our expected 2017 production at Millstone and have started hedging 2018 production
- We plan to limit our hedging of 2018 production until we see the outcome of pending legislation in Connecticut

Earnings Guidance

- Now, to earnings guidance at Dominion Energy
- Operating earnings for Q3 2017 is expected to be between $0.95 and $1.15 per share, compared to operating earnings of $1.14 per share for Q3 2016
- Positive factors for Q3 compared to last year include the addition of Questar operations
- Negative factors compared to last year include a return to normal weather, lower earnings from Cove Point due to the roll off of one of our import contracts, higher PJM's electric capacity expenses, and lower investment tax credits from solar investments

Dividend Rate

- Dominion Energy's operating earnings guidance for the full year of 2017 remains $3.40 to $3.90 per share
- As we discussed on our last earnings call, we believe operating earnings for 2018 will increase by at least 10% over 2017 driven primarily by earnings from our Cove Point export facility, which will be in service later this year
- With the planned growth across all of our business segments, we expect a 6% to 8% compound average growth rate in earnings off a 2017 base through 2020
- Not only is this one of the best growth rates in the industry, but coupled with our stated intent to grow our dividend rate greater than 8% annually beginning next year Dominion Energy provides investors with one of the best total return opportunities in the industry

Summary

So let me summarize my financial review

Second quarter operating earnings were $0.67 per share landing in the upper half of our guidance range

Third quarter operating earnings guidance is $0.95 to $1.15 per share

In 2018, operating earnings are expected to be at least 10% above 2017

And our 2017 to 2020 compound earnings growth rate to be 6% to 8%

Thomas F. Farrell II

Business Highlights

Performance

- Strong operational and safety performance continued at Dominion Energy
- All of our business units either met or exceeded their safety goals through H1
- I'm pleased that our employees set an all-time low OSHA Recordable Rate of 0.66 last year and have a goal of improving on that record this year
- Our nuclear fleet continues to operate well
- The net capacity factor of our six units through Q2 was over 96%

Growth Plans

- Now for an update on our growth plans
- Construction of the 1,588-megawatt Greensville County Combined Cycle Power Station continues on time and on budget
- As of June 30, the $1.3B project was 47% complete
- All three gas turbines, the gas turbine generators as well as the steam turbine generator and casings have been placed on their foundations
- All three heat recovery steam generators have been set with modules loaded
- The air-cooled condenser is over 60% complete
- Greensville is expected to achieve commercial operations late next year
- We have a number of solar projects under development and we continue to see demand for renewables from our customers including data centers, military installations, and the state government
- Three of these facilities, totaling a 119-megawatt achieved commercial operations during Q2

Virginia and North Carolina

- In total, we've announced 438-megawatts that will go into service this year and expect to add another 200 megawatts by the end of next year bringing our gross operating portfolio to 1,800 megawatts, about 700 megawatts of which will be in Virginia and North Carolina

Operating License Extension

- We've begun the process to seek operating license extensions for our four nuclear units in Virginia
- Earlier this year, the Virginia General Assembly enacted legislation establishing that the spending on these efforts, which could be up to $4B reaching into the next decade, will be recoverable through a separate rate rider
- The General Assembly also stated the construction of one or more new pump storage electric generating facilities in Southwest Virginia is in the public interest with costs also recoverable through a rider
  - We are evaluating a number of options and expect to have sites selected later this year

Agreement with DONG Energy of Denmark

- In July, we announced that we'd signed an agreement with DONG Energy of Denmark, a global leader in offshore wind development to build two six-megawatt turbines off the coast of Virginia Beach
- The two companies are now refining agreements for engineering, procurement, and construction
- Dominion Energy remains the sole owner of the turbines, which is targeted for completion in 2020
  - We plan to seek wider recovery in Virginia for the project

Electric Transmission Projects

- We have a number of electric transmission projects at various stages of regulatory approval and construction
- Through H1, $327mm of assets have been placed into service
- We plan to invest $800mm in our electric transmission business this year and every year thereafter for at least the next decade
- Our strategic underground program continues at Power Delivery
- Earlier this year, the Virginia General Assembly affirmed its support for the program, and clarified the standards by which the distribution line would be prioritized

Electric Sales Growth

- We plan to invest up to $175mm per year in this program to reduce the number of outage locations and their duration during major events
- We see improving prospects for electric sales growth in Virginia
- Weather normalized electric sales were up about 2% for H1, led by strong increases in sales to data center and residential customers

New Customer Connections

- New customer connections in H1 were 7% higher than last year
- We also connected five new data centers in Q2, bringing the YTD total to 8%
- In addition, anticipated increased federal spending on defense will provide strong support for the Virginia economy, which is the largest recipient of defense dollars in the nation

Cove Point Liquefaction Project

- All of these factors support our expectation that annual electric sales growth of at least 1% will continue
- Progress on our growth plan for gas infrastructure continues as well
- Our Cove Point Liquefaction Project is now 95% complete and remains on-time and on-budget

Engineering and Procurement

- Engineering and procurement is essentially finished
- Structural steel and large diameter piping installation are coming to completion and the post installation pipe testing is essentially complete

- Both phases of the operator simulator training have been successfully completed

Synchronization

- Synchronization of a steam turbine generator to the existing plant generation grid will be completed this month
- Over 90% of the project systems are now in the commissioning phase in line with our schedule
- As we work towards commercial in-service later this year, we will bring the project to a state of ready for start-up this quarter, and construction will reach essentially complete status

LNG

- On July 24, FERC provided authorization for hydrocarbon entry into four additional project areas
- We have received authorization from the Department of Energy to export LNG produced during commissioning
  - We have an agreement with a third party to provide the commissioning natural gas and to export commissioning LNG from a facility
- Finally, Q4 will provide a period of sustained production of LNG prior to achieving commercial in-service date later this year

Supply Header Project

- We are continuing to work toward commencement of construction on the Atlantic Coast Pipeline and the related Supply Header project
- On July 21, FERC issued its file environmental impact statement
- The report was favorable and concluded that all environmental impacts will be effectively mitigated and there would be no significant public safety impacts
  - We expect to receive the final certificate from FERC in the early fall
- We are in the process of securing all the necessary water crossing and other federal and state permits and expect to complete that process later this year

ACP

- ACP and Supply Header have essentially completed the design and engineering, executed the construction contract, and completed over 84% of materials procurement
- We remain on-track to start construction later this year and expect completion of the Atlantic Coast Pipeline and the Supply Header in H2 2019
- We have an additional seven pipeline growth projects underway with well over $750mm of investment
- Our keys project was completed earlier this year, and we expect four more to be completed by year end
- We are also investing nearly $300mm per year in our local gas distribution companies in three states through our infrastructure replacement programs
  - These costs are recoverable through rate rider programs in all three states

Appalachian Basin

- We are seeing continued interest in expansion projects driven by new power, industrial, and LDC loads throughout our system and expect to secure at least three or four new growth projects this year and significantly more through 2020 throughout our entire footprint including our traditional Appalachian Basin, our new Western system and our expanding Eastern footprint, which has direct access to the fast-growing Mid-Atlantic and Southeast U.S. markets

Summary

So to summarize, our business delivered strong operating and safety performance in Q2

Construction of the Greensville County project is on time and on budget

Construction of the Cove Point liquefaction project is nearly complete, and commissioning is well underway

We received a final environmental impact statement and continue to work toward commencement of construction of the Atlantic Coast Pipeline and the Supply Header Project

As we complete our major projects, we will deliver strong earnings growth starting next year

MLP Structure

- As Mark stated earlier, we expect earnings growth of at least 10% in 2018, and a diverse set of positive factors will support continued growth in years to come
- Because of our unique MLP structure, our superior cash flows will also allow a dividend growth rate at Dominion Energy higher than 8% per year
- You can expect more clarity on our long-term growth plan and ongoing dividend policy at this fall's investor conferences

QUESTION AND ANSWER SECTION

<Q - Michael Weinstein>: Hey, I was wondering if you could go through how you're dealing with the environmental opposition to the Atlantic Coast Pipeline within Virginia. What kind of deals have been reached with the opposition at this point?

<A - Thomas F. Farrell II>: I'm not sure I understand your question entirely. But there's no deals to be reached with the opposition. We're going through the permitting process as we have for the last two-and-a-half years. We'll get our FERC permit in the fall and it's a matter of going through. There's public hearings that will be held on the water permits in Virginia this month. They had them last month in North Carolina and those permits will be issued later in the fall and we will start construction in November. No deals to be struck with anyone.

<Q - Michael Weinstein>: Okay. So it doesn't sound like there is anything – any significant opposition that you're dealing with. Is that a fair statement or?

<A - Thomas F. Farrell II>: There's certainly some vocal opposition in some isolated localities, but overall, folks in Virginia support the pipeline as they do in West Virginia, North Carolina and we expect to get all the necessary permits later this fall.

<Q - Shahriar Pourreza>: Just real quick on ACP. Is there a point you need a quorum at FERC before construction shifts into 2018 or are you confident that you could start constructing in November? And then as you sort of think about incremental growth opportunities with the project, how should we sort of think about the next set of priorities? Is it starting with compression, upsizing through compression or maybe an extension of the pipeline through surrounding states?

<A - Thomas F. Farrell II>: Thank you, and good morning. We'd like to see FERC commissioners impaneled in September, would be our best guess on when that'll happen and that would allow us – no later than September is our best guess on when that'll happen, and that would allow us to start construction on this particular schedule. We won't talk about potential expansion opportunities until after we've received our FERC permit. And then, we will sit down and talk to folks.

<Q - Shahriar Pourreza>: Okay. That's helpful. And then, just a question on DM here, is it definitive that you need equity in 2018 or can you sort of finance this first ceremonial drop with Cove Point cash flows maybe looking at some investment grade debt at the DM level. So, how should we think about the first drop in 2018?

<A - Mark F. McGettrick>: Shah, it's Mark. Now, we're going to need a drop and some equity in 2018, not significant. But I think if you do the math, cash flows on coverage is very strong for us at DM well into 2018. But right now, we anticipate a drop and we want to get more liquidity in that stock anyway, there is limited trading on it. So, our ability to put more shares out, I think are advantageous.

<Q - Shahriar Pourreza>: Got it. That's helpful. And then just lastly, a lot of back and forth with the headlines in the media on Millstone and – especially with the recent governor order, can you just maybe just talk a little bit about some of the back and forth we've seen in the media, and then how far or how willing you are to provide financials on the asset? Thanks.

<A - Thomas F. Farrell II>: Good morning. There's been obviously lots in the press about what's going on in Connecticut legislature. We're working very hard on that project in the legislation. As long as they're in session, we will be working on it, and we think there are prospects to have that legislation be adopted during the course of this legislative session. The governor's issued an executive order you referenced calling for a study. We don't feel the need to – for a study to be conducted, but we will certainly participate in the study. I think it's pretty clear what's necessary in Connecticut, and we'll let it play its course.

<Q - Stephen Calder Byrd>: Wanted to just follow up on the last question on Connecticut. Do you have a sense for the process or timeline for this to play out just so we can try to follow the milestones along the way?

<A - Paul D. Koonce>: Stephen, good morning. This is Paul Koonce with the Generation Group. The session ended officially on July 7. They went into special session on July 28. It really comes down to what happens and how do they close their budget deficit. Two weeks ago, the House approved a union concession package. Monday, the Senate approved the same union concession package, which closes the budget deficit by a substantial amount. So, it really is up to the House and the Senate in Connecticut to continue to work to close their budget deficit. That could play out over the next several weeks we expect, but hopefully they will come to conclusion by Labor Day. But it's a legislative process in August, it is a difficult month to get people together. So, I'd say weeks, but we think that they're making progress.

<Q - Stephen Calder Byrd>: Okay. And the study that is underway, is that essentially – do we have a sense for how much time that will take to complete and how that sort of factors into this process?

<A - Paul D. Koonce>: Yes, I'll just comment on that. This is the governor's executive order, he's asked the Department of Energy and Environment to conduct the study. As we've said publicly, we think the time has passed for conducting studies, but be that as it may. The Department of Energy and Environment is to report out to the legislature next January. So, that's part of the legislation that was approved by the Senate, does not take legislative action. So, he's taken steps himself to move that forward. But, as the Senate bill 106 called for was action, and that's really what we think is necessary at this stage.

<Q - Stephen Calder Byrd>: Okay, understood. And then just shifting gears, if I could, to the development on offshore wind. At a high level, could you talk to the growth potential here and the economics and how you see the future of offshore wind? Could this become a significant contributor in the state? How should we think about the growth potential there?

<A - Thomas F. Farrell II>: Well, this first two turbines are test turbines. They will be built in the area that's been designated that we have the lease rights to. It's about 25 miles, 26 miles offshore of Virginia Beach, so the turbines won't be visible. We've been working on this for a number of years, long, many years trying to find a partner who would give us the kind of certainty we needed on the cost to protect our customers. So that we could go to our commission, because it will need commission approval to authorize the construction of the turbines. They are – will be subject to rider recovery.

If the turbines demonstrate that they work well in these waters and produce the kind of capacity that we expect, then it's up to 2,000 megawatts of offshore wind that would be available. We're building a lot of solar as well. Our IRP calls for up to 5,000 megawatts of solar. Solar uses a lot of land, and that's beginning to become obvious to people as maybe not quite as obvious to folks in the West, where vacant land is abundant. It's a little more obvious to folks in the East, where vacant land is not quite as abundant. So we're exploring all of our options to meet our customers' demands for decades to come. That's part of why we're looking at the relicensing of North Anna and Surry as well, and pump storage in the Virginia mountains.

<Q - Steve Fleishman>: Hey, Tom. The 2017 earnings range is still pretty wide. So, I guess any kind of commentary or thought toward kind of where you're heading in that range and when you might be able to narrow it?

<A - Mark F. McGettrick>: Steve, this is Mark. No additional commentary really. We typically don't change our ranges that we establish at the beginning of the year. And we give the quarterly guidance to see where we land. So we don't anticipate changing the range. Would also say that in Q3 – we're a weather-sensitive company, as we've already talked about, we're down $0.10 to weather through H1 and Q3 is the most sensitive we would be to weather, both positive and/or negative depending on how that turns out. So that can move us. But I think for now and probably through the remainder of the year, we will keep that range as is and just report the actuals as we move through.

<Q - Steve Fleishman>: Okay. Maybe the more important question though is you're kind of targeting your growth rate off the midpoint, or excuse me, off that range. So where you end up could have a big swing in future 2018, 2019. So is it still fair to use the midpoint of the range in thinking about that growth rate you're giving for the future?

<A - Mark F. McGettrick>: Yes, it is.

<Q - Jonathan Philip Arnold>: Can I ask on just the Connecticut and Millstone strategy? You say you're going to stay unhedged pending an outcome. If I understand the proposed measure correctly, it was going to enable maybe half of Millstone to be covered. So why not hedge the other half in the meantime or are you thinking you might have something more comprehensive as an outcome?

<A - Mark F. McGettrick>: Jonathan, this is Mark. I mentioned in the prepared remarks that we have started hedging 2018, but that we were going to limit that hedge until the outcome of the legislation. So to your point, we would expect that a portion of that output needs to be hedged, even if it's not bid into a future auction process. We're working on that now and I'll have a disclosure on that in Q3.

<Q - Jonathan Philip Arnold>: Okay. Great. I must have misheard the prepared remark. Can I ask – we were just looking at the solar slide and it looked like, in the last quarter you were expecting these projects to all be late 2017, and the North Carolina 79-megawatts of capacity came forward into Q2, what happened there? And is that the same project and how must that benefit the quarter?

<A - Paul D. Koonce>: Jonathan, this is Paul Koonce with Generation. Actually, we're sort of right on schedule. So we had a full year plan, the plan is moving on schedule. So, no change.

<Q - Jonathan Philip Arnold>: So that wasn't pulled forward from the late timing of last quarter?

<A - Paul D. Koonce>: No, it was not.