Definitions
Financial Definitions

**EPS:** Net Income / Shares Outstanding

**Dividend Payout Ratio:** Dividend / Earnings Per Share (EPS)

**Dividend Yield:** Annual Dividend Paid / Stock Price

**ROE:** Net Income / Average Stockholders’ Equity

**Total Return:** (Price Change + Dividend) / Purchase Price

**P/E Ratio:** Stock Price / Actual or Projected EPS
Quiz Question!

Pick one the stock that is the best “value”

<table>
<thead>
<tr>
<th>Company</th>
<th>Share Price</th>
<th>EPS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Viking Wind</td>
<td>$20.00</td>
<td>$1.00</td>
</tr>
<tr>
<td>Bronco Solar</td>
<td>$50.00</td>
<td>$5.00</td>
</tr>
<tr>
<td>Red Raider DSM</td>
<td>$8.00</td>
<td>$0.50</td>
</tr>
</tbody>
</table>
Bronco Solar

Represents the best value as it has the lowest P/E

<table>
<thead>
<tr>
<th>Company</th>
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<th>EPS</th>
<th>P/E Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Viking Wind</td>
<td>$20.00</td>
<td>$1.00</td>
<td>20x</td>
</tr>
<tr>
<td>Bronco Solar</td>
<td>$50.00</td>
<td>$5.00</td>
<td>10x</td>
</tr>
<tr>
<td>Red Raider DSM</td>
<td>$8.00</td>
<td>$0.50</td>
<td>16x</td>
</tr>
</tbody>
</table>
Investor Perspective
Why is the Investor Perspective Important?

- Investors own the company
- Companies need access to capital markets
  - Equity
  - Debt
  - Preferred securities
  - Hybrid securities
Types of Investors

- **Sell-Side** – provide research & recommendations
- **Buy-side** – buy and sell securities to make money
  - Mutual funds
  - Hedge funds
  - Pension funds
  - Insurance companies
- **Hedge funds** – a subset of buy-side investors
  - Active traders (holding period is often short)
  - Will go long or short
  - Use margin to increase returns
  - Frequently event driven
Investment Styles

- Growth
- Value
- GARP
- Income
- Total Return
- Index
- Technical
- Event driven
## Investor Requirements

| Equity Investors | Want: | ➢ Dividend  
➢ Dividend growth  
➢ Stock price growth |
|------------------|-------|----------------|
| Debt Investors   | Want: | ➢ Interest & principal  
➢ No drop in bond value  
➢ No drop in credit rating |
| Rating Agencies  | Judge: | ➢ Risk of making interest and principal payments |
Short Selling

• Investors profit from a decline in a security’s price
• Theory - “Sell high and Buy low”
• The loss potential from short selling is infinite
• Process:
  – Investor borrows shares through a broker
  – Investor sells shares
  – Later the investor must repurchases the shares in the open market to replace the borrowed shares, this is referred to as “Covering the Short”
  – Investor is responsible for paying for dividends on the stock during the short period
Key Evaluations Factors by Investors

- Management credibility
- Effective business strategy
- Attractive EPS growth
- Reliable cash flow
- Strong balance sheet
- Economic / Industry Trends
- Corporate governance
- Innovative products / services
- Attractive dividend
- Special situations
Tools Used by Investors

- FERC filings
- SEC filings
- Investor presentations
- Company meetings
- Develop company models to project earnings/cash flows
  - By subsidiary
  - By power plant or major asset
- Compare projected earnings/cash flows to current valuation to determine whether to buy or sell stock
Credit Rating Agencies
Role of Credit Rating Agencies

- Independent evaluators of credit
- Assign ratings
  - Company – overall credit worthiness of issuer
  - Individual security being issued
- Evaluate risk of default – failure to make payments
  - Interest
  - Principal
- Evaluate risk of loss – difference between principal and interest received discounted to date of default
- Credit ratings impact financing costs
Credit Rating Analysis Factors Based on S&P’s Criteria

**Business risk**
- Country risk and macroeconomic factors
- Industry
- Competitive position
  - Regulation
  - Markets
  - Diversification
  - Operating efficiency
  - Management
  - Governance
- Profitability/peer comparison

**Financial risk**
- Accounting characteristics
- Financial policies and risk tolerance
- Capital structure
- Cash flow protection
- Liquidity

The degree of a firm’s business risk sets the parameters of financial risk it can afford at any ratings level.
Key Credit Metrics

Funds from operations

__________________________
Debt

Funds from operations

__________________________
Interest expense

__________________________
Debt

__________________________
Debt + Equity

Funds from Operations (FFO) = net income + depreciation + amortization + deferred taxes + other non-cash items
Credit Ratings – S&P and Moody’s

- “AAA” or “Aaa” – Highest credit quality
- “AA” or “Aa”
- “A” or “A”
- “BBB” or “Baa” – Investment grade
- “BB” or “Ba” – Non-investment grade
- “B” or “B”
- “CCC” or “Caa”
- “CC” or “Ca”
- “C” or “C”
- “D” or “D” – Default
Investor Valuation
## Analyst Expectations for Xcel Energy

Mean analyst forecast projects an EPS CAGR of ~6.0%

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>XEL Guidance</td>
<td>$2.37 - $2.47</td>
<td>Not Given</td>
<td>Not Given</td>
</tr>
<tr>
<td>Analyst Range</td>
<td>$2.40 - $2.48</td>
<td>$2.55 - $2.63</td>
<td>$2.70 - $2.80</td>
</tr>
<tr>
<td>Mean Forecast</td>
<td>$2.43</td>
<td>$2.59</td>
<td>$2.74</td>
</tr>
<tr>
<td>Implied Growth *</td>
<td>5.7%</td>
<td>6.6%</td>
<td>5.8%</td>
</tr>
</tbody>
</table>

* Based on 2017 ongoing EPS of $2.30
## Sell-side Analyst Recommendations

*Updated May 11, 2018*

<table>
<thead>
<tr>
<th>Firm</th>
<th>Rating</th>
<th>FY2018 EPS</th>
<th>FY2019 EPS</th>
<th>FY2020 EPS</th>
<th>Price Target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wolfe Research</td>
<td>Hold</td>
<td>$2.41</td>
<td>$2.60</td>
<td>$2.75</td>
<td>$47.00</td>
</tr>
<tr>
<td>BAML</td>
<td>Buy</td>
<td>$2.48</td>
<td>$2.61</td>
<td>$2.70</td>
<td>$50.00</td>
</tr>
<tr>
<td>UBS</td>
<td>Hold</td>
<td>$2.41</td>
<td>$2.57</td>
<td>$2.74</td>
<td>$46.00</td>
</tr>
<tr>
<td>Evercore ISI</td>
<td>Hold</td>
<td>$2.40</td>
<td>$2.60</td>
<td>$2.75</td>
<td>$46.00</td>
</tr>
<tr>
<td>Morgan Stanley</td>
<td>Buy</td>
<td>$2.43</td>
<td>$2.61</td>
<td>$2.72</td>
<td>$50.00</td>
</tr>
<tr>
<td>Deutsche Bank</td>
<td>Hold</td>
<td>$2.45</td>
<td>$2.60</td>
<td>$2.75</td>
<td>$49.00</td>
</tr>
<tr>
<td>RBC</td>
<td>Hold</td>
<td>$2.41</td>
<td>$2.59</td>
<td>$2.73</td>
<td>$49.00</td>
</tr>
<tr>
<td>Wells Fargo</td>
<td>Buy</td>
<td>$2.45</td>
<td>$2.60</td>
<td>$2.80</td>
<td>$51.00</td>
</tr>
<tr>
<td>Macquarie Research</td>
<td>Hold</td>
<td>$2.42</td>
<td>$2.58</td>
<td>$2.74</td>
<td>$47.00</td>
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<tr>
<td>J.P. Morgan</td>
<td>Buy</td>
<td>$2.42</td>
<td>$2.57</td>
<td>$2.72</td>
<td>$49.00</td>
</tr>
<tr>
<td>SunTrust Robinson</td>
<td>Hold</td>
<td>$2.43</td>
<td>$2.57</td>
<td>$2.70</td>
<td>$45.00</td>
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<tr>
<td>KeyBanc</td>
<td>Hold</td>
<td>$2.45</td>
<td>$2.60</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Mizuho</td>
<td>Buy</td>
<td>$2.40</td>
<td>$2.63</td>
<td>$2.76</td>
<td>$47.00</td>
</tr>
<tr>
<td>Morningstar *</td>
<td>N/A</td>
<td>$2.40</td>
<td>$2.55</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>CFRA</td>
<td>Hold</td>
<td>$2.45</td>
<td>N/A</td>
<td>N/A</td>
<td>$49.00</td>
</tr>
<tr>
<td>Argus</td>
<td>Buy</td>
<td>$2.43</td>
<td>$2.60</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td><strong>Consensus</strong></td>
<td>-</td>
<td><strong>$2.43</strong></td>
<td><strong>$2.59</strong></td>
<td><strong>$2.74</strong></td>
<td><strong>$48.00</strong></td>
</tr>
</tbody>
</table>

* Morningstar uses a 1-5 star rating system, with Xcel Energy currently at two stars. Low = overvalued, High = undervalued

** Consensus EPS estimates exclude CFRA
Stock Price Performance YTD
Updated May 31, 2018

- Xcel Energy: -5.4%
- Regulated Peers: -6.2%
- Total Peer Group: -4.0%
- NASDAQ: 7.8%
- S&P 500: 1.2%
P/E Ratio
Updated May 31, 2018

Based on 2018 EPS estimates
PCG suspended its dividend
Dividend Payout Ratio
Updated May 31, 2018
Factors Driving Utility Valuations in 2018

- Rising interest rates
- Tax reform
  - Adverse impact on cash flows
  - Pressure on credit ratings
- Large scale utility equity issuances putting pressure on sector
  - Southern
  - Duke
  - PPL
  - Dominion
  - Entergy
  - FirstEnergy
  - NiSource
  - Centerpoint
  - Sempra
Significant Company Issues

- **Scana** – abandoned construction of two nuclear units
- **Southern** - construction of two nuclear units; sale of Gulf Power; Kemper
- **NextEra** – acquisition of Gulf Power
- **FirstEnergy** – bankruptcy of FirstEnergy Solutions
- **Sempra** – acquisition of Oncor; wildfire liability
- **PG&E** – wildfire liability; dividend suspension
- **Edison** - wildfire liability
- **Eversource** – hostile bid for Connecticut Water; Northern Pass
- **CenterPoint** – acquisition of Vectren; Enable
- **Dominion** – revised MLP tax policy; acquisition of Scana
- **PPL** – United Kingdom business valuation
- **AEP** – approval of Windcatcher wind project
- **AEE** – Missouri legislation
"XEL is replacing the earnings-neutral fuel portion of its electric customer bills with rate-based wind and gas plants. XEL was the first to propose and fully implement the “Steel for Fuel” strategy, and we have completely missed this business and regulatory turnaround...While the rate base growth benefits are obvious, in the near term, this strategy should boost XEL’s O&M expenses and maintenance capex as its coal plants need to cycle to back the intermittent wind resource. However, gradual retirements of coal plants and lower staffing of existing units should allow for even more cost cutting and thus higher realized ROEs." Angie Storozynski, Macquarie – May 11, 2018

"Despite XEL's strong start to 2018 from an earnings perspective, a headwind has materialized with the Colorado PUC dismissal of the PSCo electric rate case. This eliminates the potential for interim rates in 2018, although XEL described the event as a de minimis drag to 2018 earnings and reiterated 2018 guidance of $2.37-$2.47. Overall, the long term growth strategy remains intact, but we note a fair number of regulatory approvals and project execution being hurdles to sustaining top of the EPS range performance." Jonathan Arnold, Deutsche Bank – April 27, 2018
We saw Xcel Energy’s (XEL) 4Q update as largely constructive. Indeed, contrary to many concerns XEL presented itself as a net beneficiary of tax reform, as the loss of bonus depreciation raises rate base by ~$1.8bn, offset by about $500m in capex reduction. As a result, we expect rate base growth to rise from its historical base level of 5.5% to 6.5%. Moreover, including the CO Clean Energy Plan capex (~$1.3bn) mgmt sees CAGR of 7% as likely.” Julien Dumoulin-Smith, Bank of America Merrill Lynch – February 8, 2018

"Xcel Energy (XEL): upgrading from Equal-weight to Overweight, with a $48 price target (implying 11% upside). XEL leverages low-cost wind to increase capital spending while driving customer bills lower and generating energy in a more sustainable way. As a result of this dynamic, the company offers above average earnings growth and faces less burdensome regulatory hurdles, while appealing to ESG investors globally — a trend that we believe could potentially drive improved valuation for the company." Stephen Byrd, Morgan Stanley – Feb. 13, 2018

"Mizuho upgrades Xcel Energy to Buy fromNeutral driven by an increase in our 2018-2021 EPS estimates resulting from higher capital spending at the utilities. Additionally, we believe there additional upside opportunity given the high likelihood the Colorado Energy Project gets approved…We estimate $0.08-$0.10 of accretion if the CEP is approved, assuming the project is funded with a mix of debt and equity.” Paul Fremont, Mizuho – Mar. 27, 2018
What is the impact of tax reform? Impact on credit metrics and liquidity? How will regulators treat the lower revenue requirements? Impact on financing plans and equity needs? Impact on your credit ratings?

Impact of the ALJ recommendation in your Colorado natural gas rate case and read through to next electric case? What is the potential to get a multi-year rate plan in Colorado? Impact of lower equity ratio? Impact on EPS growth rate?

How competitive are your wind projects? Is there potential for more wind ownership projects? Impact of tax reform?

What is the status of the Colorado Energy Plan? Impact on growth rate? How would you finance CEP?

Approval of SPS wind proposal?

Why not increase the 5-6% EPS growth objective?

Ability to close ROE gap by 50 bps? Impact on EPS growth rate?

What initiatives will ensure flat O&M? Can you deliver declining O&M?

M&A view?