US Electric Utilities & IPPs

'Ya Gotta Believe' NY Prices Are Heading Higher

Equities

Americas

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Julien Dumoulin-Smith
Analyst
julien.dumoulin-smith@ubs.com
+1-212-713 9848

Michael Weinstein
Associate Analyst
michael.weinstein@ubs.com
+1-212-713 3182

Paul Zimbardo
Associate Analyst
paul.zimbardo@ubs.com
+1-212-713 1033

New York capacity and power prices poised for further recovery

We look for the NYISO market to further improve as both ETR's Fitzpatrick (851MW) and EXC's Ginna (583MW) are slated to retire in Fall 2016 and Spring 2017, respectively. We have revised up our NYISO capacity prices further, seeing the outlines of the latest mini-boom in the state, following NRG's recent retirement of its Huntley and Dunkirk coal units totalling 900MW. While unclear what offsetting assets could yet return from mothball status to capture the pricing uplift, we see prices heading materially higher across the state in the near-term, particularly in the upstate region. Net-net, we conservatively forecast a Summer 2017 NYISO capacity print of $7/kW-mo up from ~$3.50/kW-mo this last summer 2015. We include a full table of our regional capacity estimates and sensitivity by company below.

Is a deal still possible? Doubtful in our view.

While mgmt confirmed that New York and ETR have had conversation in recent weeks to save its Fitzpatrick plant, rhetoric out of the state suggests it does not understand the depth of the plant's losses, blaming the company for sacrificing jobs to the detriment of its 'bottom line'. While New York has nominally suggested it will pursue legal and regulatory avenues possible to keep the plant open (which is what ETR has wanted all along), we suspect the ~$60 Mn/yr deficits projected by mgmt is just too much to accommodate ($225-275 Mn avoided FCF drag through 2020 vs. retiring at end of 2016). With just 600 jobs at the plant and $17 Mn/yr in local taxes, the deficit remains too wide to strike a deal with benefits to the state. Furthermore, without an obvious reliability need to keep the plant around, NYISO has not extended a comparable reliability RSSA arrangement as it did previously with EXC's Ginna.

Who benefits the most? The classic IPPs, including TLN, NRG, and DYN

Given the latest retirements, EXC and ETR have meaningfully reduced their sensitivities to this market, with the remaining sensitivity primarily attributable to IPPs including TLN, DYN, and NRG. We attribute NRG's outperformance yesterday in large part to the ETR retirement, with NRG having the largest nominal portfolio at ~3.8GW. While we provide specific capacity price improvements below, we suspect NYISO Zn A prices could improve nicely as well having seen highs last year when talk initially emerged around nuclear retirement potential.

What does this all mean for Indian Point? Cheap gas remains the problem

We maintain our generally bearish expectations for delivered gas basis in the downstate region of NY with the forthcoming in-service of both Constitution pipeline and Millennium expansion bringing cheap Marcellus gas. We know at least one if not two new CCGTs intend to be built in the state on the back of the cheaper delivered gas in the Lower Hudson Valley (LHV) zone near Indian Point. As such, we suspect overall economics for ETR's Indian Point asset remain backwardated despite the latest retirements.

How about Indian Point? NY at logger heads with ETR

With NY State governor Cuomo calling the decision to close the Fitzpatrick plant 'callous' (ignoring the clear cash flow deficits), we suspect any deal around extending IP's life for a nominal period remains off the table. We suspect NY and ETR will remain at logger heads over the plant's potential relicensing for an additional 20-years (we see a ~10-year extension as likely a sufficient deal to entice ETR). From a strategic perspective, we don’t necessarily see ETR as poised to abandon its IPP strategy despite just two remaining restructured nuclear assets (although reduced volatility in its entirely regulated remaining nuclear portfolio would be well received).

Updating our New York Capacity Forecast:

We include our latest update to our capacity price forecast. We reflect a meaningful improvement in pricing, notably for Summer 2017, where we could well see further upside given the confluence of both the Fitzpatrick unit retiring in Fall 2016 and then Ginna in Spring 2017. While taken together the NYISO sensitivities would drive a $5-6/kW-mo uplift, we suspect other offsetting impacts will materialize at these higher prices including imports from adjacent regions to partially backstop high priced summer capacity obligations. We also revise up our winter capacity price forecast. On a blended basis, we see prices as trending upward by north of ~$20/kW-yr YoY in 2017. This should also work to sustain LHV capacity prices (including for Indian Point) as we suspect prices here should compress in the ~2018 period as new CCGT build of CPV Valley's plant is contemplated for in-service, pushing the region to clear once more with the balance of the state ('Rest of State' market). We see the retirements as likely pushing additional new CCGT capacity to pursue new entry, focusing Advanced Power's proposed Cricket Valley CCGT (also near Indian Point).

We see the twin nuclear retirements in 2017 driving a bumper year for capacity and power prices

Our prior forecast had called for a flattish profile in 2017, with a decline in 2018 with new CCGT entry. We now see a $3/kW-mo bump from our prior forecast settling out a higher overall level in 2018 despite the new plant entry.

The further question remains the timing of plant retirements during the Winter of 2016-2017 and to what extent the strip auction will reflect the unit retirements fully (or only partially).

Figure 1: NYISO Capacity Price Forecast – Pushing Estimates Up for Nuclear Retirements

NYISO ICAP Forecast	2010	2011	2012	2013	2014	2015	2016E	2017E	2018E
NYC Forecast									
Summer ICAP ($/kW-month)	12.90	13.54	11.70	14.80	16.24	15.50	15.50	15.50	15.50
$/kW-yr	154.80	162.48	140.40	177.60	194.88	186.00	186.00	186.00	186.00
$/MW-day	424	445	385	487	534	510	510	510	510
Winter ICAP ($/kW-month)	4.65	4.60	2.70	4.50	7.54	8.45	6.67	6.67	6.67
$/kW-yr	55.80	55.20	32.40	54.00	90.48	101.40	80.04	80.04	80.04
$/MW-day	153	151	89	148	248	278	219	219	219
Annualized ($/kW-yr)	105.20	105.04	90.00	121.88	144.50	140.14	133.02	133.02	133.02
$/MW-day	288	288	247	334	396	384	364	364	364
NY - Rest of State (RoS)									
Summer ICAP ($/kW-month)	2.47	0.55	1.25	4.20	5.15	3.50	4.25	7.00	5.00
$/kW-yr	29.64	6.60	15.00	50.40	61.80	42.00	51.00	84.00	60.00
$/MW-day	81	18	41	138	169	115	140	230	164
Winter ICAP ($/kW-month)	1.75	0.39	0.15	0.82	2.58	2.90	1.25	4.25	4.50
$/kW-yr	21.00	4.68	1.80	9.84	30.96	34.80	15.00	51.00	54.00
$/MW-day	58	13	5	27	85	95	41	140	148
Annualized ($/kW-yr)	22.60	5.16	9.74	33.64	47.02	35.10	39.00	68.00	56.00
$/MW-day	62	14	27	92	129	96	107	186	153
Lower Hudson Valley Estimate									
Summer ICAP ($/kW-month)					9.96	8.50	8.07	8.07	5.00
$/kW-yr					119.52	102.00	96.81	96.81	60.00
$/MW-day					327	279	265	265	164
Winter ICAP ($/kW-month)					-	5.90	3.73	3.73	4.50
$/kW-yr					-	70.80	44.76	44.76	54.00
$/MW-day					-	194	123	123	148
Annualized ($/kW-yr)					-	86.40	70.78	70.78	57.00
$/MW-day					-	237	194	194	156

Source: Platts, UBSe

New England also poised to have retirement as soon as Spring 2017

Also occurring in the Northeast is Entergy's planned retirement of the Pilgrim (683MW) nuclear unit. While the plant could conceivably retire as soon as February, 2017, management has not yet decided as to whether it will be able to execute on repurchasing its capacity obligations for the subsequent two year period through mid-2019. We emphasize the combination of higher capacity prices alongside a tighter market framework suggests a meaningful potential premium will need to be offered to close out the position. We're biased to believe the plant remains open through its existing obligations.

Sensitivities by Company

We include our sensitivities by company. While NRG has historically had the highest sensitivity given its large portfolio in the state (explaining its outperformance yesterday), we actually estimate TLN as having the great exposure to the state on a per share basis following its recent close of the MachGEN portfolio acquisition. We emphasize upstate assets will likely see the greatest upside from retirements.

Figure 2: Capacity Price Sensitivity by Company & EBITDA Uplift YoY into 2017

NY Capacity (MW)	NRG	ETR	EXC	PEG	DYN	CPN	TLN
Rest of State	1,628	-	837	774	1,108	-	1,080
Lower Hudson Valley	758	2,069	-	-	-	-	-
New York City	1,366	-	-	-	-	121	-
Long Island	-	-	-	-	-	231	-
Total	**3,752**	**2,069**	**837**	**774**	**1,108**	**352**	**1,080**
Sensitivity to $1/kW-Month Change in Capacity Pricing							
Rest of State	20	-	10	9	13	-	13
Lower Hudson Valley	9	25	-	-	-	-	-
New York City	16	-	-	-	-	1	-
Long Island	-	-	-	-	-	3	-
Total	**45**	**25**	**10**	**9**	**13**	**4**	**13**
2017 UBSe EBITDA	2,746	3,887	6,307	4,303	1,247	2,121	801
% Change	**1.6%**	0.6%	0.2%	0.2%	**1.1%**	0.2%	**1.6%**

New York City							
Last year's winter price ($/kW-Month)	8.5						
This year's winter price UBSe ($/kW-Month)	5						
Price Delta	3						
	NRG	**ETR**	**EXC**	**PEG**	**DYN**	**CPN**	**TLN**
In-City Capacity (MW)	1,366	-	-	-	-	121	-
Sensitivity to change in price (6 month impact)						*Contracted (JFK)*	
New York City	28.3	-	-	-	-	-	-
% Change to '17 EBITDA	**1.0%**	0.0%	0.0%	0.0%	0.0%	**0.0%**	0.0%

Putting the Estimates Together for RoS Changes							
2016 Annualized	39						
2017 Annualized	66						
Net Change ($/kW-yr)	27						
	NRG	**ETR**	**EXC**	**PEG**	**DYN**	**CPN**	**TLN**
EBITDA Uplift	**99**	**55**	**22**	**21**	**29**	**9**	**29**

Source: Company reports and UBS estimates

EXC/ETR: Shortening the life of Ginna further

Exelon and Rochester Gas & Electric (RG&E) filed a joint proposal with the New York Public Service Commission (PSC) on October 21st regarding the Reliability Support Services Agreement (RSSA) for Exelon's R.E. Ginna nuclear plant. **The most significant change in the new proposal is that the RSSA runs through March 2017 compared with September 2018 previously.** The latest agreement sets compensation at $15.4Mn per month plus $11.5Mn on March 31, 2017; this compares negatively with the previous agreement of $17.5Mn per month. As part of the agreement RG&E receives 70% of energy and capacity revenue and Ginna keeps the remaining 30%. In contrast the previous proposed agreement had 85% of revenues flowing to RG&E. The revenue sharing change is a positive revision that should offset the the lower set monthly compensation. Total revenues under the RSSA are subject to a floor of $425Mn and cap of $510 whereby RG&E has to compensate for any deficiency or is subject to refunds by June 30, 2017.

Latest Ginna joint proposal reduces length of support agreement to March 2017 from September 2018 previously.

After March 2017 RG&E is required to issue a RFP which Ginna can participate in and potentially be awarded with a new RSSA. As part of the filings in a partially redacted document Exelon commented that "it appears highly unlikely that there will be an incentive for Ginna to return to the market after RSSA termination." In an October 22nd interview with Bloomberg Exelon CEO Chris Crane stated that Ginna will retire after the duration of the RSSA and we continue to see a transmission solution as the most likely. RG&E has already disclosed that it is working on just that: the Ginna Retirement Transmission Alternative (GRTA) which should be completed in 2018-2020. Entergy has opposed support agreements in New York recently and it remains to be seen how intervenors view this latest joint proposal. Regardless, we believe the writing on the wall is clear: single-unit merchant nuclear assets will continue to be challenged economically given the current power and gas outlook. (Case No. 14-E-0270)

The NY PSC has stated that the number one issue currently is finding a solution to mitigate the rate increase on rate payers which is currently +2% based on the refundablel rates.

Further details are available in our recent notes on Ginna below:

2/20/15 Gimme a Number for Ginna
2/17/15 Saving The Nukes? Ginna.

Figure 3: Ginna – Mini Model – Latest RSSA runs through March, 2017

Ginna w/ RSSA Deal	2015	2016	2017
Capacity (MW)	581	581	581
Capacity Price ($/kW-yr)	35.1	32.5	34.7
Capacity Payments	18	16	18
Market Power Prices ($/MWh) w/ 10% Prem to Zn A	37.86	32.54	33.70
Generation (TWh)	4.70	4.70	4.70
Energy Revenue ($ Mn)	178	153	158
Under new Subsidy Scheme			
RSSA (Fixed for 85% of Output)	140	210	210
RSSA (+15% on Market)	86	23	24
Total Revenues	226	233	234
Implied Revenue ($/MWh)	48.08	49.56	49.74
Nuclear Fuel Capex ($/MWh)	6.00	6.30	6.62
Nuclear Fuel ($ Mn)	(28)	(30)	(31)
Gross Margin	198	203	203
Direct O&M (w/ Premium to CENG)	(135)	(135)	(135)
Other O&M (w/ Premium to CENG)	(26)	(26)	(26)
Total Costs	(161)	(161)	(161)
Implied $/kW-yr	278	278	278
EBITDA	36	42	41
Maintenance Capex (30% Prem)	(39)	(39)	(39)
FCF	(3)	3	2

Source: Company reports and UBSe

NY politicians oppose FitzPatrick close; dis-economies of scale hits nuke fleet

Plant will not refuel next Fall, opting to retire amidst low capacity and power prices

Entergy plans to close its FitzPatrick nuclear asset by 1/31/17 but top state politicians plan to fight the move. NY Governor Cuomo has been a vocal critic of Entergy's handling of its nuclear assets and pledged to "pursue every legal and regulatory avenue in an attempt to stop Entergy's actions and its callous disregard". ETR confirmed months of discussions with NY officials and media reports tie the administrations of Cuomo and US Senator Charles Schumer to the talks which involved the outlook for Entergy's Indian Point Energy Center (IPEC). ETR disclosed $35Mn overhead per Northeast plan, half of which is indirect and requires allocation to the other remaining units.

Mgmt expected a $225-$275Mn cash drag from operating the plant vs retirement through '20. The closure of two nuclear assets within 30-days raises questions about cost allocation to the remaining nuclear assets (both regulated and unregulated) for overhead, etc, as we had assumed a greater cash deficit from the plant (eg- not all costs can be avoided). The book value for Pilgrim and FitzPatrick collectively is $94Mn which will be expensed through 2019. ETR did not provide EWC adjusted EBITDA guidance (previously $470-$490Mn in 2015E-2017E before divestitures/closures), as this would singularly focus on the one-remaining 'merchant' plant, Indian point. We emphasize our estimates reflect declining capacity prices (excluding our latest revision, driven by the plant's very own retirement).

Figure 4: Fitzpatrick – Projected FCF – Expected to close by January 2017

Fitzpatrick	2015E	2016E	2017E	2018E	2019E	2020E
Capacity (MW)	838	838	838	838	838	838
Generation (GWh)	7,194	7,194	7,194	7,194	7,194	7,194
Capacity Factor (%)	98%	98%	98%	98%	98%	98%
Market Price (Unit Contingent Discount Applied), $/MWh	$37	$32	$32	$31	$31	$32
Weighted Avg. Hedged Power Price ($/MWh)	$41	$43	$34	$31	$31	$32
Capacity Payments - NYISO (RoS), $/kW-yr (UBSe)	$48	$27	$28	$21	$21	$20
Revenue ($ Mn)	344	335	275	244	248	250
Nuclear Fuel ($/MWh)	4.1	6.3	6.2	6.1	6.1	6.1
Fuel Cost ($ Mn)	(29)	(45)	(45)	(44)	(44)	(44)
Non-Fuel Production Cost ($ Mn)	(149)	(157)	(160)	(160)	(160)	(160)
NYPA Value Sharing	(24)	-	-	-	-	-
Fixed O&M (Proportionally allocated)	(28)	(57)	(44)	(44)	(44)	(44)
Nuclear Refueling Expense	(30)	(31)	(22)	(22)	(23)	(23)
Taxes other than Inc.	(25)	(26)	(23)	(23)	(24)	(24)
EBITDA Margin ($ Mn)	57	19	(19)	(49)	(46)	(46)
EBITDA Margin ($/MWh)	7.96	2.67	(2.60)	(6.82)	(6.46)	(6.36)
Est. D&A	(46)	(37)	(40)	(41)	(40)	(40)
EBIT	11	(18)	(58)	(90)	(87)	(85)
Interest Allocated	(4)	(4)	(4)	(4)	(4)	(4)
Pretax Income	7	(22)	(62)	(94)	(91)	(89)
Taxes (assume 37%)	(3)	8	23	35	34	33
Net Income	8	(10)	(35)	(55)	(53)	(52)
Cash Flow Adjustments:						
D&A	46	37	40	41	40	40
Addback Nuke Fuel	29	45	45	44	44	44
CFO	84	73	49	30	31	31
Nuke Capex	(63.52)	(64)	(64)	(64)	(64)	(64)
Fuel	(54)	(55)	(57)	(59)	(60)	(62)
Total Capex	(117)	(119)	(121)	(122)	(124)	(126)
Free Cash Flow	(33)	(46)	(72)	(93)	(93)	(95)
FCF / MWh	(5)	(6)	(10)	(13)	(13)	(13)

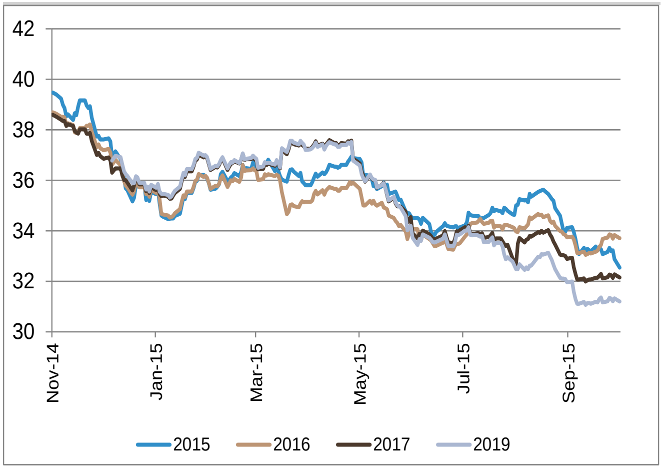
Source: Company reports and UBSe

Where do the commodities stand now?

While ATC power prices remain depressed in the upstate market, showing sharp backwardation, we emphasize downstate Zone G prices remain elevated vs. our expectations for future delivered gas prices to the region. We include Spark spreads of Zone G vs. Dom-South prices +$0.10/MMBtu basis to reflect hypothetical sparks on a new CCGT (currently under construction *across* from Entergy's plant).

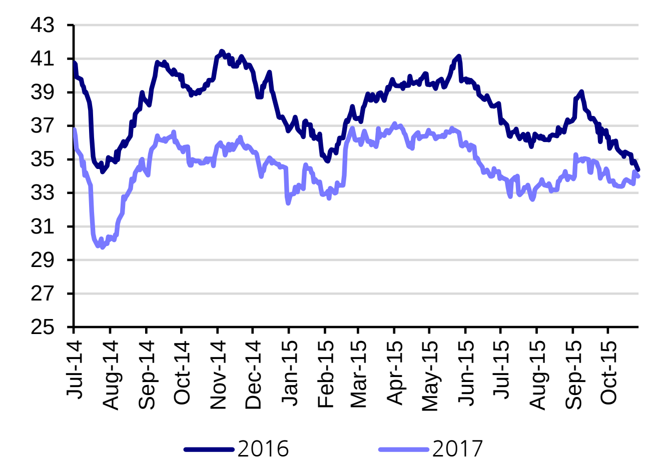
We remain bearish on power price trends – nuclear retirements should alleviate some of these pressures

Figure 5: NY-Zn A – ATC Power price ($/MWh)



Source: Platts

Figure 6: NY-Zn G – Spark Spread @7.2 Heat Rate ($/MWh)



Source: Platts

Further details are available in our recent notes on NYISO capacity below:

De-Nuclearizing the Northeast
The New York Capacity Swing
The Nuke Retirements are coming
Taking Down Coal in the Empire State
NYISO ICAP Capacity Auction Preview

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Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%
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Source: UBS. Rating allocations are as of 30 September 2015.
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Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Calpine Corporation[2, 4, 6, 13, 16]	CPN.N	Buy	N/A	US$15.41	02 Nov 2015
Dynegy, Inc.[4, 6, 16]	DYN.N	Buy	N/A	US$19.70	02 Nov 2015
Entergy Corp.[16]	ETR.N	Sell	N/A	US$68.55	02 Nov 2015
Exelon Corp.[4, 6, 16]	EXC.N	Neutral	N/A	US$28.37	02 Nov 2015
NRG Energy Inc.[16]	NRG.N	Buy	N/A	US$13.36	02 Nov 2015
Public Service Enterprise Group[16]	PEG.N	Neutral	N/A	US$40.62	02 Nov 2015
Talen Energy Corp[5, 16]	TLN.N	Neutral	N/A	US$8.95	02 Nov 2015

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