

# US Electric Utilities & IPPs

## Jamming to the Nashville Rock

### Equities

Americas  
Electric Utilities

#### Visiting the Music City to hear the latest tunes on utilities

We hosted our latest regulator forum this week to discuss key debates with a variety of industry stakeholders. First, the focus remains nationally on Net Energy Metering (NEM) reforms, poised to begin to rollback such tariffs across a wide range of jurisdictions. Second, gas safety and citing bottlenecks remain a clear focus, as execution of pipeline permitting has been highlighted by recent challenges. Third, nuclear and the ability to 'save' units through new state level carbon regimes was among the most debated topics; we expect a renewed focus on meshing environmental markets with energy & capacity to prove the critical power market reform in 2H16. We are surprised at the widespread interest in the topic – with both ISO-NE and PJM poised to proactively address the topic with meaningful stakeholder processes beginning in the August timeframe. Look for leadership importantly from ISO-NE on reflecting carbon prices in energy market bids (rather than via the existing low prices in the RGGI market); in contrast, PJM's efforts appear to be focused on capacity market options to support carbon-free baseload assets. Complementing carbon is the continued meaningful scaling of renewable (solar) additions, with much more RFP activity than we had previously expected (despite projections for continued weak load growth), with meaningful upside surprises to expectations from GA, NY, and MA in the next week.

#### What are the equity implications from the forum? Constructive backdrop

Overall, we perceive the regulatory backdrop as still readily constructive, with more limited downside on authorized ROEs, no meaningful discussion of capital structure, and continued support for execution of particularly gas-related priorities. In fact, we see risks declining around Net Metered Solar nationally. On a discrete basis, we see FE as poised to gain approval of its efforts in Ohio, saving its balance sheet. We see the widespread focus at both PJM and among member states to provide a 'solution' for nuclear revenues as positive for EXC. Meanwhile, doubts on MI legislation in 2016 are a headwind for CMS & DTE. Further, continued concerns in GA & MS around execution on time for Vogtle and Kemper reiterate our caution on SO & SCG. We note the backdrop in AZ remains favorable for PNW, but we remain on the sidelines amidst the ongoing rate case.

#### Gas infrastructure citing gaining substantially greater attention

Beyond the NEM reforms contemplated, we note a renewed focus on gas pipeline certification as well as safety efforts amidst a renewed push to ensure adequate gas infrastructure to feed the country's electric grid dependence on natural gas. To illustrate this point, we emphasize the appointment as NARUC President-elect Rob Powelson from PA to effectively spearhead this effort across the organization in 2017. We note multiple recent pipeline delays as well as outright rejection in New York State has renewed understanding of PUC citing regulations.

#### Gas safety too is gaining national attention – with two recent regulations.

We emphasize two new rules issued this year to ratchet up focus on safety. Starting in March PHMSA issued new regulations focused on pipeline safety, while new legislation sponsored by Fred Upton of MI drove a renewed focus on gas storage safety among a host of other items. Broadly, we expect the accelerated pace of gas main replacement alongside other retrofits to continue to drive substantial positive revisions in capital spending across not just gas utilities but drive strategies for electric utilities keen to expand into gas infrastructure as illustrated in recent SO-AGL and DUK-PNY.

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## **NARUC conference is focused on national Net Metering (NEM) Reform**

We look for NEM reform to accelerate in 2H, likely reducing the attractiveness of economics across wide range of states in the coming year as a set of common practices for reforms are adopted. While the effort does not necessarily suggest no removal of NEM is a 'bad' outcome, we perceive a wider interest at the conference in reducing NEM compensation across a wide variety of efforts.

## **Retaining the Nuclear Portfolio: How to *fix* the carbon problem?**

Among the most important themes emerging in the Power sector is a clear focus on environmental markets – and the ability to recover carbon-free attributes provided by nuclear plants, such as the latest Zero Emission Credit (ZEC) proposal in New York. If successful – and upheld at FERC – we would expect states such as Ohio, Pennsylvania, Connecticut, and even New Jersey to potentially follow. We emphasize the latest complaint over EXC's efforts to get paid for the carbon aspects of its nuclear portfolio is likely to prove among the more decisive in preventing this trend from becoming a precedent. We note historic willingness by parties including FERC to accommodate Renewable Energy Credits (RECs) as an acceptable supplementary source of revenue bodes well for ZECs to garner acceptability. While Illinois, with its substantial nuclear exposure remains less probably following stalled efforts, we believe investors fail to appreciate the ability for such efforts to expand to other states; moreover, we emphasize investor reaction to the development in New York remain quite skeptical, despite our expectations for formal approval of this construct next Monday August 1<sup>st</sup> alongside wider nuclear reforms. Further, we see FERC as poised to uphold these efforts on appeal as well, seeing it as an environmental externality rather than explicit out of market subsidy.

## **What shape could nuclear support take in Pennsylvania? RPS reform.**

While we would not expect an explicit ZEC effort in PA, we could well envision a shift in the RPS standard to include Uprates of nuclear plants among other forms of compensation to encourage nuclear generation. Seeing uprates as likely off the table, this could yet prove a more contentious focus for the most vulnerable plants in the state including both Three Mile Island (TMI) and TLN's Susquehanna.

## **Power Markets**

### **PJM: Burgeoning Modest Reforms to Capacity Performance**

We perceive continued efforts to tweak the latest Capacity Performance (CP) implementation in PJM to reflect seasonality and reduced penalties for failure to participate for both Demand Response (DR) as well as renewable resources. We note the primary driver of projected YoY improvement in capacity prices under CP is tied to the substantial purge of DR participating as 'base capacity' today, which is unlikely to be fully transitioned MW-for-MW. *The risk here is removing the 'teeth' in the CP uplift on pricing; this could reduce the pricing benefits before they are ever implemented?*

### **MISO: Awaiting New Capacity Arrangement**

We continue to await a final debate at MISO on which capacity market reforms it will ultimately pursue. With two proposals (Market Monitor and MISO Staff), we suspect IPPs will bias towards the 3-year forward market pushed by MISO staff, providing the forward looking revenue visibility desired even if still allowing for

regulated entities to participate in this new structure. We suspect this will prove just the starting point for the latest series of market reforms to be adopted in the MISO market as efforts are scrambled to save remaining Illinois merchant generation in Zone 4. Given the forthcoming retirement of the Clinton nuclear unit, we suspect prices could meaningfully improve. We look for this filing in August to FERC, providing a positive catalyst for DYN.

## Ohio

### **Can FirstEnergy succeed with its latest distribution rider? We think so.**

We continue to believe that FirstEnergy will be successful in its pending petition for distribution rider mechanism. While the company has followed up on the Staff proposal for ~\$130 Mn for a 3-5 year period with its own more expansive proposal for ~\$568 Mn/yr over a full 8-year period, we continue to believe a compromise can be found largely splitting the difference (say ~\$200 Mn as the pre-tax revenue requirement for the \$130 Mn figure proposed by Staff).

While many remain concerned of whether the State Supreme Court will uphold this decision following a series of rejections recently from this court against AEP and DP&L of their respective efforts to receive 'transition' payments. While the new FE structure is technically a distribution modernization rider, with exemption from the 'Significant Excessive Earnings Test' (SEET) used to limit the overall realized ROEs in the state. Bottom line, we are not surprised to see FE shift in rebuttal testimony towards the Staff proposal in an effort to avoid the pitfalls of the earlier FERC indication it would not *waive* review of any contract tied to the FES generation business. We continue to expect resolution of the current docket this Fall.

### **Rates from FE would remain in effect until rejected; Stay is low likelihood.**

While many investors remain quite cautious on this new structure, we emphasize that in order for a Stay to be executed once approved by the PUCO, the petitioning party would need to post a bond equal to the total revenues forgone during the period of time. As such, we question if parties against the effort would be able to post such a large sum of money even if ultimately returned. We believe the temporary award of revenues from the PUCO (even if ultimately rejected by the courts) would prove a key transient factor to support their investment grade credit ratings into 2017.

### **Focusing on the credit quality story – the focus shifts towards S&P.**

While we and the Street have largely been focused on Moody's required 14% FFO/Debt, we emphasize the ~12% FFO/Debt required by S&P is the growing focal point. To this end, among the growing questions is whether a two-notch difference between the holding company and operating companies would be permitted as a transient factor amidst efforts to bolster the aggregate credit quality. This could potentially allow some downside support to the company attempting to walk a tight rope on aggregate leverage, while keeping the utilities within the critical investment grade ratings bucket. A final question remains precisely what toll regulators would exact on the utilities should they drop below investment grade?

## **FE's go forward strategy: de-emphasize generation**

We note a clear desire by FE to distance itself from the generation business, not just seemingly for purposes of the credit rating agencies, but also for purposes of perception related to the ongoing complaint at FERC on the original PPA structure between the generation business and the utility (effectively blocked by FERC given its willingness to remove its blanket waiver – and evaluate the contract). We continue to expect a meaningful break in corporate strategy on this Friday's 2Q call; in fact, we would not be surprised to hear a delineation of a wider sell, shut, and re-regulate strategy to provide a pathway towards a de-risk utility balance sheet (and hence more latitude in FFO/Debt metrics). In particular, we suspect generation in West Virginia could well see the subject of ratebasing remaining coal assets further revisited amidst this effort. We note the recent plant closures effect for 2019 announced last week are likely only the first in a further wave of potential plant retirements.

## **But could FE still seek a nuclear strategy later even with distribution?**

While the current backdrop continues to stress the need to seek revenues from the distribution utility, we would not be surprised to see a subsequent effort to address the distressed nuclear plants in the state. Given FE's continued ownership in 4 units, we would expect mgmt. to put a hard line for Ohio to either provide adequate revenues to support the plants or allow their gradual retirement; we suspect the former will ultimately prove the avenue taken (despite the clear opposition to the Clean Power Plan, CPP, implementation taken up by Ohio Governor Kasich).

## **DPL: Gaining Clarity on the Way Forward (AES +ve)**

We are notably less concerned on prospects for DPL (AES) as we expect the company to largely 'remove' itself from the latest ESP rates following their rejection by the Ohio Supreme Court. We understand that the company can elect to remove its ESP rates and revert back to its prior 'regulated' tariffs, maintaining above-market compensation to DPL; this would require the company to pay Suppliers their stated rates without an explicit passthrough on bills. Further, this would allow for recovery of DPL generation's fuel in rates. We note the continued single structure of the utility and generation readily enables these prior rates to go into effect. While not easy to implement, this appears the near-term answer to swift implementation after the latest court rejection. The fate of its pending extension of the now defunct tariff remains unclear (the ESP III filing); we would expect an entirely new filing to prove forthcoming to comply with the latest Ohio court decision. Net-net, visibility on a way forward is a positive to shares. We expect AES to maintain its 2016 EPS guidance pending resolution of this matter (particularly should the rate impact prove less impact than removing the entire above-market payment at ~\$0.10 annualized and just ~\$0.05 in 2H16).

## **AEP: Pursuing a Sale? No word yet.**

While mgmt. at AEP guides investors to expect developments later this year at EEI on the fate of its ongoing sale process despite taking bids for the portfolio of late, we maintain our confidence the company will ultimately divest its generation portfolio. We perceive the latest seeming hesitation to a degree of caution on what could ultimately be approved by the PUCO in FirstEnergy's latest case – and prospects for any similar deal for AEP.

## **Nascent effort for full re-regulation in Ohio? We don't think so.**

The question in the state remains whether there is palatability for a full re-regulation of the state – or re-regulation of select assets. While we suspect not, this remains a subject open to some debate and potential 2017 legislative effort. We note this effort appears pushed more by AEP than FirstEnergy.

## **Georgia:**

### **Will SO pursue yet another nuclear plant?**

The focus in the near term remains on whether rate recovery will be granted on SO's nascent efforts to build a greenfield new nuclear plant in Western Georgia (along the Alabama border) to be known as Stuart 1&2. The initial recovery appears to be quite controversial among commissioners and promises to be a point of contention at the upcoming rate proceed on Thursday around its Integrated Resource Plan (IRP). With existing pipeline capacity already running through the site it would appear SO is prepared to expand via gas if rejected as well.

### **Procurement: Looking at up to 1.6GWs of Solar**

Among the most surprising solar developments of late is the potential for a 3-year cumulative 1.6GW solar procurement, as the commission remains surprisingly committed to shifting the fuel mix in the state. We emphasize this is up from the initially contemplated 500 MWs for the 3-year period and confirms that the Southeast will likely prove among the more robust regions of at least new growth, if not absolute growth for the utility-scale solar sector through the near-term.

### **GA Power: layoffs to support 3-year rate stayout plan under AGL deal**

Georgia Power committed to a three year rate stayout as part of the deal to acquire the AGL system, with the latest round of layoffs in recent weeks aimed to support this end of maintaining its ROE through the period.

## **Washington**

Among key developments from the state is a potential focus on new legislation in 2017 focused on pursuing wider coal divestment and an increased RPS, consistent with efforts in adjacent Oregon in the latest session. We emphasize the Governor has been outspoken in his desire to see transition in the state away from Coal. We note Puget Sound continues to have an ownership in the MT coal plant, Colstrip which garners continued in-state attention.

## **Arizona:**

### **Prospects for smoother solar relationship? Yes.**

While the solar interests failed to find common ground with the utilities at the outset of the latest rate case with PNW, we emphasize the latest shift in regulatory approach with the hiring of Former FERC Chair Jon Wellinghof at SCTY has meaningfully shifted perceptions. While fundamental policy agreements remain quite clear given inability to tackle at least basic principles in earlier settlement, we perceive substantially less political risk as past years through the election cycle.

### **Could ROE become more formulaic? Yes look to water utility developments**

As part of the latest slew of ongoing rate cases, we emphasize recent clues have emerged as to the treatment of rate cases. Notably, prospects for a more formulaic

banding approach to California appear to be appealing in an effort to reduce the cost of litigating cost of capital cases frequently. This would be a positive development, reducing regulatory risk.

## Hawaii

Focus in the state remains on HEI's stand-alone prospects following the failed deal with NEE. We note LNG prospects remain dim in the state following the decline in oil prices as well as statements from Governor Ige in opposition to fossil fuels.

On the solar front, we emphasize addressing NEM reform and providing a future for islands to sell solar systems that are structured as self-supply remains important. Notably both RUN and SCTY offer products that are competitive without NEM. We note the likely forthcoming implementation of AMI in the state and subsequent implementation of Time of Use (ToU) rates adds a further risk to even those systems that have been grandfathered as midday rates Net Metered back to the grid could well decline.

## Mississippi

### Defining a period of sustain operations

In evaluating the project performance, a key emerging question is precisely just how long the plant will need to be in operation in order to be adequately deemed as such for rate recovery. While the plant is nominally targeted for in-service in ~3Q, mgmt. does not anticipate filing until year-end at the earliest. We understand the plant will need to run consistently for ~6-weeks in order to fulfill this requirement.

### Focused on MS PSC itself – budget issues limit staff

We further note that Commission has suffered multiple budget cuts, following a decision to fund the PSC through the general legislative budget and not directly through utility payments. The Commission currently does not anticipate emergency rate relief for Kemper, nor directly passing along Kemper's cost overruns to rate payers.

### Expanding Renewables via Long-Distance Transmission

Among the key debates across the Southeast in an effort to expand renewable penetration is whether to pursue renewable imports into the region rather than building in region as an effective procurement answer. In particular the MS PSC is awaiting a proposal from PEGI regarding a HVDC transmission line intended to run bring excess wind capacity from (East) Texas, through Louisiana, to Mississippi (near the AL border). PEGI has already filed proposal in TX, but has yet to provide the MS PSC with concrete information regarding the project. The MS PSC expects to receive the filing in October of this year, but cautions that approval process might likely take longer, as budget constraints and Kemper limit staff time for new projects. We note that MS PSC does not require the transmission line to be fully contracted. The transmission line will extend 200 miles into Mississippi, ending around the Columbus area. As such, the terminus will be in the SO footprint.

**Should the southeast use long-distance transmission access to wind to complement solar?**

## Maryland

### Looking for further commission turnover; concerns on rate inflation

Continued meaningful reform of the PSC continues to occur; the backdrop remains will the new commission prove as focused on consumer bill inflation? We think yes. Anne Hoskins (D) will step down at the end of this week with Tony O'Donald replacing her. Mr O'Donald is a long time legislator from Southern MD. Formerly involved in the Republican leadership, he will start his new appointment on August 1, 2016. The MD PUC does not have a requirement to maintain balanced partisan representation, such that this change will shift the commission further Republican. The most recent appointment follows the trend of Republican appointments. Last year, R-Gov. Hogan appointed Jeannette B. Mills, former BGE Chief Customer Officer, and, in January of this year, his former Energy Advisor R-Michael Richard.

We note Mr. Richards has been outspoken in the need to address ratepayer affordability and has expressed concerns on growth including smart meter recovery. With EXC having filed its first rate cases after the acquisition close in the state, the key question remains whether it will prove successful in its efforts to improve its earned ROE. We note the current proposal seeks to raise rates materially with a 20% hike; the question is whether the magnitude of the hike and subsequent hikes sought to improve its earned ROE as well as accelerated capex will drive EXC into the same persistent under-earning cycle experienced by POM? We suspect at least the delayed rate cases resulting from the deal as well as true up on the delayed AMI recovery should improve the outlook immediately.

## New York

### Looking for a bold affirmation on nuclear's place from New York

While the ZECs have received most of the attention as of late, we note that the NY PUC will also vote on RPS this coming Monday, Aug 1. The most recent proposal awaiting approval by the commission includes the goal of 50% renewables in the electricity generation mix by 2030. We note that nuclear generation does not qualify for RPS and that ZECs will have run out at that point. Nevertheless, given that nuclear generation currently provides 26% of total electricity generation, NYS could likely see zero carbon generation provide over 60% of total electricity generations in the years following up to the 2030 RPS deadline.

### 'Opt-out' Community Choice emerges in New York; will it happen?

Community Choice Aggregation (CCA) represents another contentious issue currently discussed by the NY PUC. Initially started in the state through a pilot program in Westchester, CCA has now become a state-wide program, before results regarding the success of the pilot program could ever be reviewed. CCAs allows counties to purchase electricity from a separate source than the main utility provider to support their customer base. So far CCA programs have been approved in MA, OH, CA, NJ, RI and IL. We note the wild success of CCAs in Illinois have dramatically changed the retail shopping landscape, with nearly a substantial portion of consumers covered under such contract at some point in time. We see this as a controversial move amidst efforts to empower individual consumers to pursue their own energy consumption preferences.

Meaningful shift in retail landscape could yet emerge

## **Taking a deeper looking at ESCOs: reforms potentially ahead too**

In tandem to the CCA development, we point to the substantial number of ESCOs in NY. Currently, there exist about 200 ESCOs in the state, approximately ~50 of which are registered as ESCOs but have no customers, with the remaining ~150 consisting of either utility subsidiaries and small independent power producers. We note that market participants have voiced concerns regarding both the small producers who lack adequate risk controls as well as the utility affiliates whose fair marketing practices with their utility parents are under scrutiny.

## **Nevada: Waiting Anxiously for Real Reform**

### **We see the state as potentially turbulent in coming months**

We perceive both the solar Net Energy Metering (NEM) rules as well as wider discussion of restructuring as on the table for discussion in the state. Despite the paucity of publically traded exposure in the state, we continue to see its efforts on both fronts as cautious for regional utilities. Notably, we see the direction in Arizona as quite different, with NEM poised to decline modestly via demand charges as well as with the firm previous rejection of restructuring.

### **Restructuring: How quickly and who? Wider headwind**

We see the continued efforts by the data center Switch and Las Vegas casinos as continuing to exit utility as cautious datapoints, illustrating that they can indeed pursue this avenue should the exit payments merit the annualized savings. With supply charges poised to remain quite modest across the West given subdued natural gas prices and meaningful deployment of solar, we could well see many other commercial and industrial entities seek to capitalize on a legacy 15-year old restructuring law to exit the system. We suspect this point will become increasingly flesh out as legacy renewable (and thermal) supply obligations entered into by NV Energy are more clearly articulated.

### **Ballot on Market Deregulation & potentially Solar NEM this Fall**

Supported by Switch and other industry participants hoping to exit the Nevada electricity market, we see high likelihood for constitutional amendment on market deregulation on the upcoming ballot. We note, however, that the amendment has to pass the ballot twice in order to affect resolution, indicating that market deregulation cannot be achieved before 2020 along this path. This is alongside the latest grandfathering efforts in the state, which would be included on this November's election as well. We emphasize there remains some ambiguity as to whether or not the NEM piece will be put on the ballot this Fall or not still depending on whether it is a petition or a referendum.

## **New Jersey**

### **Smart meters are emerging focus: benefit to PEG, FE, and EXC (POM)**

It appears the state is increasingly focused on a deployment of smartmeters across its full array of utilities. While positive to not just PSE&G as it seeks to continue its high-growth trajectory, we see this as a potential positive development for FE and EXC as they seek to accelerate growth opportunities; we emphasize for FE's JCP&L service territory, this represents the greatest opportunity of any of its service territories to accelerate the pace of spend as it has largely passed up stimulus-like investments pursued by PEG in recent years. Further, we see AMI as a clear avenue



for deployment for EXC as part of an effort to ensure the POM utilities contribute their respective portion to EXC's elevated 7-9% regulated EPS growth rate. *We emphasize this remains a controversial effort given past pushback on such efforts from both the Rate Counsel and BPU Staff.*

### **Gearing up for a nuclear focus in 2018? Refocusing on carbon**

PSEG and EXC have engaged in a wider effort to maintain its nuclear reform, potentially driving reforms via either a direct effort to save its remaining nuclear units (after the contemplated retirement of Oyster Creek in 2019). While sitting Governor Christie had taken NJ out of the RGGI Carbon trading program previously, we emphasize any effort in NJ could well be state specific to provide resilience to these plants in the 2018 timeframe (after the current administration's tenure).

### **Offshore wind: Coming in the next few years?**

The state appears increasingly focused on the offshore opportunities present, with 1.1GW of land leased off its shores; some of these leases are owned by DONG. We emphasize growing attention to offshore possibilities in the US, with Massachusetts poised to be the first state to potentially pass meaningful offshore requirements as part of its pending legislation. We note the limited renewable resources available to NJ put it in a particularly acute position to look towards offshore resources as avenue to meet its longer-term renewable ambitions. We flag the state is contemplating the creation of O-RECs (Offshore Renewable Energy Credits). The outlook is focused on the next 5-year outlook.

## **Michigan**

### **Will reforms happen? Something less comprehensive is possible.**

We remain quite modest in our expectations for legislation to be adopted at all this year. Given the pending close of the main session, and short Lane Duck session after the election, the window appears to continue to close. We emphasize there have been datapoints in recent months on progress between the various interest groups. As such, we increasingly believe a more modest bill could well be advocated to address issues such as the limit for what needs a 'Certificate of Need' (CON); under a reduction from the \$500 Mn minimum to ~\$200 Mn, utilities could petition for certainty on even modest sized gas plants under this approach. Further, we suspect some potential for a review of the Renewable Portfolio standard beyond current targets; the ambition has been 20% by 2025 under proposed legislation. The intractable issues remain on a reduction in the retail shopping cap from 10%. On the margin, we are less confident in a potential legislative deal. While legislation of any flavor would be constructive, timing could well be shifted out a year into 2017, albeit we note the substantial turnover in the composition of the respective legislation bodies in the state next year could impede progress as legislators are reintroduced to the subject. We continue to prefer DTE over CMS given opportunities in the midstream sector as well as discounted valuation vs. the wider regulated peer group.

## FERC

**Capacity market reforms:** Largely done for now? It does not appear there are substantial reforms under way driven by FERC for the time being. Rather, we perceive the Commission as content they have been successful in shifting compensation in restructured markets towards this revenue source *ahead* of growing renewable penetration.

**Transmission:** We're still awaiting the next fully litigated ROE case under Norman Bay. We emphasize all ROE cases in recent history (since the LaFleur Chairmanship) have been settled – and have not provided an opportunity for the new chair to leave his mark on the methodology employed. We emphasize the last set of transmission ROE reforms adopted under Order 531, including the capping ROEs within the zone of reasonableness was the last set of adjustments to the methodology; we emphasize this reform was undertaken at the time with the contributions from staff contributions from all commissioners, and a meaningful effort to address the reform suggesting there may not yet be willingness to tackle the issues

### **Composition poised to change next year: More Republicans Coming.**

With Commissioner Clark's term having ended on June 30<sup>th</sup>, we think the FERC will be left with just three Democrats in charge in 2H16. Given the need to preserve a minimum quorum of political representation, at least two new Republican appointments will be made next year (regardless of the election outcome); this could well change the tone of the commission.

## Valuation Method and Risk Statement

Risks for Utilities and Independent Power Producers (IPPs) primarily relate to volatile commodity prices for power, natural gas, and coal. Risks to IPPs also stem from load variability, and operational risk in running these facilities. Rising coal and, to a certain extent, uranium prices could pressure margins as the fuel hedges roll off Competitive Integrations. Further, IPPs face declining revenues as in the money power and gas hedges roll off. Other non-regulated risks include weather and for some, foreign currency risk, which again must be diligently accounted in the company's risk management operations. Major external factors, which affect our valuation, are environmental risks. Environmental capex could escalate if stricter emission standards are implemented. We believe a nuclear accident or a change in the Nuclear Regulatory Commission/Environment Protection Agency regulations could have a negative impact on our estimates.

Risks for regulated utilities include the uncertainty around the composition of state regulatory Commissions, adverse regulatory changes, unfavorable weather conditions, variance from normal population growth, and changes in customer mix. Changes in macroeconomic factors will affect customer additions/subtractions and usage patterns.

Risks for Empire District Electric (EDE) and Westar Energy (WR) include but are not limited to: (1) potential inability to deliver on its regulated capital expenditure program; (2) adverse political/legal/regulatory actions; (3) unfavorable weather and natural resources yield [wind generation]; (4) operational and construction risk; (5) inability to access the capital markets on attractive terms; (6) declines in customer demand and population; (7) failure to close pending M&A transactions; (8) natural disasters or accidents; (9) change in macroeconomics; and (10) other unforeseen changes. Valuation is based on the announced purchase price (from Great Plains Energy for Westar and from Algonquin Power for Empire District Electric).

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12-Month Rating	Definition	Coverage <sup>1</sup>	IB Services <sup>2</sup>
<b>Buy</b>	FSR is > 6% above the MRA.	47%	32%
<b>Neutral</b>	FSR is between -6% and 6% of the MRA.	38%	25%
<b>Sell</b>	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	Definition	Coverage <sup>3</sup>	IB Services <sup>4</sup>
<b>Buy</b>	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
<b>Sell</b>	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2016.

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

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**UBS Securities LLC:** Julien Dumoulin-Smith; Paul Zimbardo; Jeremiah Booream, CFA.

#### Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
<b>AES Corporation</b> <sup>16</sup>	AES.N	Neutral	N/A	US\$12.61	26 Jul 2016
<b>American Electric Power, Inc.</b> <sup>5, 6a, 7, 16</sup>	AEP.N	Buy	N/A	US\$69.74	26 Jul 2016
<b>CMS Energy Corporation</b> <sup>16</sup>	CMS.N	Neutral	N/A	US\$45.00	26 Jul 2016
<b>DTE Energy Co.</b> <sup>2, 4, 5, 6a, 7, 16</sup>	DTE.N	Buy	N/A	US\$98.00	26 Jul 2016
<b>Dynegy, Inc.</b> <sup>6a, 7, 16</sup>	DYN.N	Neutral	N/A	US\$16.68	26 Jul 2016
<b>Exelon Corp.</b> <sup>6a, 7, 16</sup>	EXC.N	Neutral	N/A	US\$37.09	26 Jul 2016
<b>FirstEnergy Corp.</b> <sup>7, 16</sup>	FE.N	Neutral	N/A	US\$35.89	26 Jul 2016
<b>NextEra Energy</b> <sup>2, 4, 5, 6a, 6b, 7, 16</sup>	NEE.N	Buy	N/A	US\$128.43	26 Jul 2016
<b>Pinnacle West Capital Co.</b> <sup>6a, 16</sup>	PNW.N	Neutral	N/A	US\$79.48	26 Jul 2016
<b>Public Service Enterprise Group</b> <sup>16</sup>	PEG.N	Buy	N/A	US\$45.77	26 Jul 2016
<b>SCANA Corp.</b> <sup>2, 4, 5, 6a, 7, 16</sup>	SCG.N	Neutral	N/A	US\$73.79	26 Jul 2016
<b>Southern Company</b> <sup>2, 4, 5, 6a, 6b, 7, 16</sup>	SO.N	Sell	N/A	US\$54.45	26 Jul 2016

Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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